

SPENCER MUNICIPAL UTILITIES
INDEPENDENT AUDITORS' REPORTS
FINANCIAL STATEMENTS
AND SUPPLEMENTAL INFORMATION
DECEMBER 31, 2010 AND 2009

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SPENCER MUNICIPAL UTILITIES

OFFICIALS

<u>Board of Trustees</u>	<u>Title</u>	<u>Term Expires</u>
(Before July 2010)		
Bruce Tamisiea	Chairman	6-30-2010
Dave Hultgren	Vice-Chairman	6-30-2011
Gary Tolzmann	Secretary	6-30-2012
Murray Hart	Treasurer	6-30-2013
Tom Howe	Trustee	6-30-2014
<u>Management</u>		
Steven Pick	General Manager	
Trisha Bruning	Finance Manager	
(After July 2010)		
Dave Hultgren	Chairman	6-30-2011
Gary Tolzmann	Vice-Chairman	6-30-2012
Tom Howe	Secretary	6-30-2014
Murray Hart	Treasurer	6-30-2013
Sandi Schmidt	Trustee	6-30-2016
<u>Management</u>		
Steven Pick	General Manager	
Trisha Bruning	Finance Manager	

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SPENCER MUNICIPAL UTILITIES

**MUNICIPAL ELECTRIC UTILITY
OF THE CITY OF SPENCER, IOWA**

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INDEPENDENT AUDITORS' REPORT

Board of Trustees
Spencer Municipal Utilities – Municipal Electric Utility
Spencer, IA 51301

We have audited the accompanying financial statements of the business-type activity of Municipal Eclectic Utility of the City of Spencer, Iowa (the Utility), as of and for the year ended December 31, 2010, which collectively comprise the Utility's basic financial statements as listed in the table of contents. These financial statements are the responsibility of management. Our responsibility is to express an opinion on these financial statements based on our audit. The prior year comparative information has been derived from the Utility's 2009 financial statements and, in our report dated May 6, 2010, we expressed an unqualified opinion on the respective financial statements of the business-type activity.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatements. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the business-type activity of the Utility as of December 31, 2010 and the respective changes in financial position and cash flows for the year then ended, in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated April 5, 2011, on our consideration of the Utility's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards*, and should be considered in conjunction with this report in considering the results of our audit.

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis, budgetary comparison, and funding progress for the retiree health plan information on pages 3 through 5 and pages 26 through 29 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Williams & Company, P.C.
Certified Public Accountants

Spencer, Iowa
April 5, 2011

MANAGEMENT'S DISCUSSION AND ANALYSIS

The purpose of management's discussion and analysis (MD&A) is to provide the reader with an introduction to the financial statements. Our discussion and analysis of the Municipal Electric Utility (Utility) of the City of Spencer, Iowa's financial performance provides an overview of the Utility's financial activities for the years ended December 31, 2010 and 2009.

The following information should be read in conjunction with the financial statements and the accompanying notes to the financial statements that follow this section.

2010 Financial Highlights

The Utility delivered approximately 154,300,000 kilowatt hours (kWh) of electricity to its retail customers in 2010 compared to approximately 147,100,000 kWh in 2009.

The Utility's net assets decreased by \$1,475,449 to \$46,040,980 as a result of operations and an increase in payables associated with Storefront Initiative for the year ended December 31, 2010. The final year for the Storefront Initiative program was 2010. Over \$360,000 Storefront Initiative claims, payable to the City of Spencer, were submitted in December for payment at the January 2011 Board meeting.

Overview of the Financial Statements

The balance sheets include the Utility's assets and liabilities and provide information about the nature and amounts of investments in resources (assets) and the obligations to creditors (liabilities).

The statement of revenues, expenses and changes in net assets report all revenues and expenses incurred during the fiscal year.

The Statement of Cash Flows present cash receipts, cash disbursements, and net changes in cash resulting from operations, capital and related financing activities and investing activities.

The notes to the financial statements provide the required disclosures and other information that is necessary to give the reader a complete understanding of the data provided in the statements. The notes present information about the Utility's accounting policies, material risks, obligations, commitments, contingencies and subsequent events.

Condensed Financial Information

The following condensed financial information serves as the key financial data and indicators for management, monitoring, and planning.

Condensed Statement of Net Assets

	<u>2010</u>	<u>2009</u>
Current assets	\$ 8,032,205	\$ 4,328,819
Noncurrent assets	10,454,385	14,543,991
Capital assets, net of depr.	37,285,463	38,422,154
Deferred costs	94,220	108,005
Total assets	<u>\$55,866,273</u>	<u>\$57,402,969</u>
Current liabilities	\$2,465,293	\$1,906,540
Bonds payable	7,360,000	7,980,000
Total liabilities	<u>9,825,293</u>	<u>9,886,540</u>
Invested in capital assets, net of related debt	29,305,463	29,847,154
Restricted	2,388,097	2,389,843
Unrestricted	14,347,420	15,279,432
Total net assets	<u>46,040,980</u>	<u>47,516,429</u>
Total liabilities and net assets	<u>\$55,866,273</u>	<u>\$57,402,969</u>

Condensed Statement of Revenues, Expenses and Changes in Net Assets

Sales of electricity	\$9,247,080	\$8,958,226
Other	1,035,733	679,087
Total operating revenue	<u>10,282,813</u>	<u>9,637,313</u>
Power supply costs	7,294,083	6,411,468
Distribution system maintenance	1,622,168	1,590,631
Depreciation & amortization	2,437,741	2,377,058
Customer service & administration	53,586	995,870
Total operating expenses	<u>12,307,578</u>	<u>11,375,027</u>
Operating (loss)	(2,024,765)	(1,737,714)
Interest income	366,528	489,054
Interest expense	(360,351)	(444,927)
Other income	543,139	837,719
Total non-operating revenues	<u>549,316</u>	<u>881,846</u>
Change in net assets	(\$1,475,449)	(\$1,058,442)
Net assets, beginning of year	<u>47,516,429</u>	<u>48,574,871</u>
Net assets, end of year	<u>\$46,040,980</u>	<u>\$47,516,429</u>

Financial Analysis

The Utility's total assets decreased by approximately \$1,540,000.

The Utility's gross revenues increased by approximately \$646,000 or 6.70%. The increase was partially due to a \$462,500 increase in ECA revenue which is directly related to the increase in purchased power costs and increased residential and industrial Kwh sales.

Total operating loss generated in 2010 was \$2,024,765 compared to an operating loss of \$1,737,714 in 2009.

Utility non-operating income (expense) resulted in \$549,316 of income, which was a 19% decrease from 2009 primarily due to the increase in Lieu of Property Taxes paid to the City of Spencer.

Total net income (loss) increased from (\$1,058,442) in 2009 to (\$1,475,449) in 2010.

Capital Assets and Debt Administration

Net capital assets decreased by approximately \$1,136,691 due to depreciation exceeding assets placed in service.

Spencer Municipal Utilities had invested approximately \$599,000 for the development and construction of Sutherland Generating Station Unit 4. During March 2009 Interstate Power and Light, an Alliant Energy Company, cancelled plans to construct the plant. A cash settlement was negotiated and Spencer Municipal Utilities received \$225,365 and recognized a loss of \$373,177.

Economic Factors

Retail sales increased by 3,200,000 Kwh in 2010 and Industrial sales increased by 2,300,000 Kwh in 2010, which represents an approximate 5% and 48% increase, respectively, from to 2009.

The utility adopted an Energy Cost Adjustment (ECA) for all consumption beginning September 7, 2005. The ECA is calculated monthly and is designed to recoup the additional costs of power supply from the consumer.

Contacting the Utility's Financial Management

This financial report is designed to present our citizens, customers, and creditors with a general overview of the Utility's finances and operating activities. If you have any questions or require additional information please contact the Finance Supervisor, 712 Grand Ave, PO Box 222, Spencer, Iowa 51301.

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**MUNICIPAL ELECTRIC UTILITY
OF THE CITY OF SPENCER, IOWA
STATEMENTS OF NET ASSETS
DECEMBER 31, 2010 AND 2009**

	2010	2009
ASSETS		
Current Assets:		
Cash and Cash Equivalents		
Unrestricted	\$ 828,811	\$ 681,449
Restricted	110,936	79,630
Board Designated	4,000,000	-
Consumer Deposits	74,711	59,036
Accounts Receivable (Net of Allowance for Doubtful Accounts of \$5,600)	1,194,747	1,008,401
Unbilled Usage	470,381	433,242
Materials and Supplies Inventory	640,205	679,107
Fuel Inventory	376,898	378,936
Notes Receivable - City of Spencer	25,000	659,331
Prepayments	310,516	349,687
Total Current Assets	8,032,205	4,328,819
Capital Assets:		
Plant in Service	72,044,438	71,354,350
Accumulated Depreciation	(35,954,304)	(33,572,633)
Net Plant in Service	36,090,134	37,781,717
Land	123,604	86,092
Construction in Progress	1,071,725	554,345
Total Capital Assets	37,285,463	38,422,154
Noncurrent Assets		
Noncurrent Investments:		
Unrestricted	-	62,848
Board Designated	4,500,000	8,500,000
Restricted	2,308,455	2,310,213
Notes Receivable - City of Spencer	645,930	670,930
Notes Receivable -Municipal Communications Utility	3,000,000	3,000,000
Unamortized Bond Issue Costs	94,220	108,005
Total Noncurrent Assets	10,548,605	14,651,996
Total Assets	\$ 55,866,273	\$ 57,402,969

See Accompanying Notes to Financial Statements

**MUNICIPAL ELECTRIC UTILITY
OF THE CITY OF SPENCER, IOWA
STATEMENTS OF NET ASSETS
DECEMBER 31, 2010 AND 2009**

	2010	2009
LIABILITIES AND NET ASSETS		
Current Liabilities:		
Accounts Payable	\$ 1,541,838	\$ 1,047,770
Payroll and Sales Tax Payable	31,623	18,557
Accrued Payroll and Compensated Absences	169,339	156,299
Accrued Interest Payable	27,782	29,878
Consumer Deposits	74,711	59,036
Current Maturities of Long-Term Debt	620,000	595,000
Total Current Liabilities	<u>2,465,293</u>	<u>1,906,540</u>
Bonds Payable:		
Bonds Payable	7,980,000	8,575,000
Less - Current Maturities	<u>(620,000)</u>	<u>(595,000)</u>
Total Bonds Payable	<u>7,360,000</u>	<u>7,980,000</u>
Total Liabilities	<u>9,825,293</u>	<u>9,886,540</u>
Net Assets		
Invested in Capital Assets, Net of Related Debt	29,305,463	29,847,154
Restricted	2,388,097	2,389,843
Unrestricted	<u>14,347,420</u>	<u>15,279,432</u>
Total Net Assets	<u>\$ 46,040,980</u>	<u>\$ 47,516,429</u>

See Accompanying Notes to Financial Statements

**MUNICIPAL ELECTRIC UTILITY
OF THE CITY OF SPENCER, IOWA
STATEMENTS OF REVENUES, EXPENSES AND
CHANGES IN FUND NET ASSETS
FOR THE YEARS ENDED DECEMBER 31, 2010 AND 2009**

	2010	2009
Operating Revenues:		
Residential	\$ 3,602,731	\$ 3,427,817
Commercial	4,402,309	4,775,279
Public Authorities	494,845	470,468
Sales for Resale	960,402	632,514
Energy Cost Adjustment Revenue	747,195	284,663
Penalties	20,281	18,295
Miscellaneous	55,050	28,277
Total Operating Revenues	10,282,813	9,637,313
Operating Expenses:		
Generation and Transmission		
Neal #4 Fuel and Generation	1,205,768	988,755
Walter Scott #4 Fuel and Generation	1,407,846	1,181,676
Purchased Power	4,586,423	4,155,594
Other	94,046	85,443
Distribution	1,622,168	1,590,631
Depreciation and Amortization	2,437,741	2,377,058
Customer Operations	348,432	315,504
General and Administrative	605,154	680,366
Total Operating Expenses	12,307,578	11,375,027
Operating (Loss)	(2,024,765)	(1,737,714)
Non-Operating Income (Expense):		
Interest Income on Investments	366,528	489,054
Resource Conservation	(483,166)	(202,574)
Economic Development Payment	(49,466)	(34,805)
Leased Facilities	2,143,817	1,951,047
Interest Expense	(360,351)	(444,927)
Gain (Loss) on Plant Retirements	(9,732)	4,415
Loss on Investment	-	(373,177)
Payment in Lieu of Property Taxes	(1,058,314)	(709,761)
Total Non-Operating Income (Expense)	549,316	679,272
Change in Net Assets	(1,475,449)	(1,058,442)
Net Assets at Beginning of Year	47,516,429	48,574,871
Net Assets at End of Year	\$ 46,040,980	\$ 47,516,429

See Accompanying Notes to Financial Statements

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**MUNICIPAL ELECTRIC UTILITY
OF THE CITY OF SPENCER, IOWA
STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED DECEMBER 31, 2010 AND 2009**

	2010	2009
Cash Flows From Operating Activities:		
Cash Received From Customers	\$ 10,075,003	\$ 9,780,080
Cash Payments to Suppliers for Goods and Services	(7,434,958)	(7,214,737)
Cash Payments to Employees for Services	(1,834,594)	(1,998,010)
Cash Payments for Resource Conservation	(483,166)	(202,574)
Cash Payments for Economic Development and In Lieu of Property Taxes	(1,107,780)	(744,566)
Payments Received From Leasing of Facilities	2,143,817	1,951,047
Net Cash Provided By Operating Activities	1,358,322	1,571,240
Cash Flows From Capital and Related Financing Activities:		
Acquisition & Construction of Property and Equipment	(1,182,391)	(1,936,605)
Revenue Bond Principal Repayment	(595,000)	(2,740,000)
Proceeds from Sale of Capital Assets	-	8,842
Interest Paid	(362,447)	(452,502)
Net Cash (Used) By Capital and Related Financing Activities	(2,139,838)	(5,120,265)
Cash Flows From Investing Activities:		
Payments Received on Note Receivable -City of Spencer	609,331	25,000
Loan Advances for Note Receivable -City of Spencer	-	(1,017,761)
Payments Received on Note Receivable Employee	-	950
Proceeds From Redemption of Investments	5,775,000	7,033,000
Purchase of Investments	(1,775,000)	(7,537,070)
Return on Investment	-	225,364
Interest Received From Investments	366,528	489,054
Net Cash Provided (Used) By Investing Activities	4,975,859	(781,463)
Net Increase (Decrease) in Cash	4,194,343	(4,330,488)
Cash and Cash Equivalents at Beginning of Year	820,115	5,150,603
Cash and Cash Equivalents at End of Year	\$ 5,014,458	\$ 820,115
Reconciliation:		
Cash and Cash Equivalents		
Unrestricted	\$ 828,811	\$ 681,449
Restricted	110,936	79,630
Board Designated	4,000,000	-
Consumer Deposits	74,711	59,036
	\$ 5,014,458	\$ 820,115

See Accompanying Notes to Financial Statements

**MUNICIPAL ELECTRIC UTILITY
OF THE CITY OF SPENCER, IOWA
STATEMENTS OF CASH FLOWS (CONTINUED)
FOR THE YEARS ENDED DECEMBER 31, 2010 AND 2009**

	2010	2009
Reconciliation of Operating (Loss) to Net Cash Provided by Operating Activities		
Operating (Loss)	\$ (2,024,765)	\$ (1,737,714)
Adjustments to Reconcile Operating (Loss) to Net Cash Provided By Operating Activities		
Depreciation and Amortization	2,437,741	2,377,058
Leased Facilities Income	2,143,817	1,951,047
Contributions Paid for Economic Development	(49,466)	(34,805)
Payment in Lieu of Property Taxes	(1,058,314)	(709,761)
Payment for Resource Conservation	(483,166)	(202,574)
(Increase) Decrease in Operating Assets:		
Accounts Receivable	(186,346)	107,566
Unbilled Usage	(37,139)	2,303
Materials and Supplies Inventory	38,902	(156,486)
Fuel Inventory	2,038	(19,964)
Prepayments	39,171	(22,630)
Increase (Decrease) in Operating Liabilities:		
Accounts Payable	494,068	32,837
Accrued Payroll and Compensated Absences	26,106	(48,535)
Consumer Deposits	15,675	32,898
Total Adjustments	<u>3,383,087</u>	<u>3,308,954</u>
Net Cash Provided By Operating Activities	<u>\$ 1,358,322</u>	<u>\$ 1,571,240</u>

See Accompanying Notes to Financial Statements

**MUNICIPAL ELECTRIC UTILITY
OF THE CITY OF SPENCER, IOWA
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2010 AND 2009**

Note 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

A. Organization and Basis of Accounting

The Municipal Electric Utility of the City of Spencer, Iowa (Electric Utility or Utility) operates as an independent unit of the City of Spencer and is managed, along with the Municipal Water Utility and the Municipal Communication Utility of the City of Spencer, Iowa, by a five member Board of Trustees.

The Utility follows the accounting practices prescribed through the Federal Energy Regulatory Commission for regulated utilities and proprietary fund accounting for governmental entities under accounting principles generally accepted in the United States of America.

For financial reporting purposes, the Utility has included all funds. The Utility has also considered all potential component units for which it is financially accountable, and other organizations for which the nature and significance of their relationship with the Utility are such that exclusion would cause the Utility's financial statements to be misleading or incomplete. The Governmental Accounting Standards Boards has set forth criteria to be considered in determining financial accountability. These criteria include appointing a voting majority of an organization's governing body, and (1) the ability of the Utility to impose its will on that organization or (2) the potential for the organization to provide specific benefits to, or impose specific financial burdens on the Utility. It was determined that the Utility has no component units.

The Utility is not considered to be a component unit of the City of Spencer for financial statement purposes.

The Utility's financial statements are reported using the economic resources measurement focus and the accrual basis of accounting. Revenues are recorded when earned and expenses are recorded when liability is incurred, regardless of the timing of related cash flows.

In reporting the financial activity of its enterprise fund, the Utility applies all applicable GASB pronouncements as well as the following pronouncements issued on or before November 30, 1989, unless these pronouncements conflict with or contradict GASB pronouncements: Financial Accounting Standards Boards Statements and Interpretations, Accounting Principles Board Opinions, and Accounting Research Bulletins of the Committee on Accounting Procedure.

The Utility distinguishes operating revenues and expenses from non-operating items. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with the Utility's principal ongoing operations. The principal operating revenues of the Utility are charges to customers for sales and services. Operating expenses include the cost of sales and services, administrative expenses, and depreciation on capital assets. All revenues and expenses not meeting this definition are reported as non-operating revenues and expenses.

**MUNICIPAL ELECTRIC UTILITY
OF THE CITY OF SPENCER, IOWA
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2010 AND 2009**

Note 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

B. Capital Assets and Depreciation

Capital assets are stated at original cost when first devoted to public service. Currently, such costs include labor-related expenditures, such as payroll taxes, pensions, and other fringe benefits and administrative costs for labor related to the construction of new electric facilities. In addition, net interest costs on construction debt are capitalized. During 2010, the Utility did not have construction debt so no interest expense was capitalized.

Under a joint ownership agreement with other utilities, the Electric Utility has a 1.215% undivided interest in a 644 MW electric generation station known as George Neal Generating Station Unit No. 4. The Electric Utility's 1.215% ownership interest in this plant represents a total investment of \$4,875,630 included in utility plant in service with \$4,093,801 included in accumulated depreciation. Operating costs associated with this plant and depreciation are reflected in the statement of income.

Under a joint ownership agreement with other utilities, the Electric Utility has a 1.07% undivided interest in a 790 MW electric generation station known as Walter Scott, Jr. Energy Center Unit 4, which was placed in service in 2007. The Electric Utility's 1.07% ownership interest in this plant represents a total investment of \$14,666,778 included in utility plant in service with \$1,516,433 included in accumulated depreciation. Operating costs associated with this plant and depreciation are reflected in the statement of income.

Replacements and betterments of capital assets are charged to capital assets. Routine maintenance and repairs are charged to expense as incurred.

Depreciation is provided on a straight-line basis. Current depreciation expense is approximately 3.36% of the original cost of depreciable electric plant in service.

The estimated useful lives used to depreciate assets by class are as follows:

Infrastructure	20-33 years
Building and improvements	20 years
Equipment	5 years

C. Accounts Receivable

Accounts receivable are stated at the amount the Utility expects to collect from outstanding balances. The Utility provides for probable uncollectible amounts through a charge to earnings and a credit to valuation allowance based on its assessment of the current status of individual accounts. Balances that are still outstanding after the Utility has used reasonable collection efforts are written off through a charge to the valuation allowance and a credit to accounts receivable. Changes in the valuation allowance have not been material to the financial statements.

**MUNICIPAL ELECTRIC UTILITY
OF THE CITY OF SPENCER, IOWA
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2010 AND 2009**

Note 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

D. Inventories

Inventories are valued at the lower of cost or market. The average cost method is used for determining the cost of materials and supplies inventory. Inventories are recorded as an expenditure or, if applicable, capitalized when consumed.

E. Unamortized Bond Issue Costs

Unamortized debt issue costs are amortized over the life of the debt on a straight-line basis which approximates the effective interest method.

F. Net Assets

Net assets represent the difference between assets and liabilities in the financial statements. Net assets invested in capital assets, net of related debt, consists of capital assets, net of accumulated depreciation, reduced by the outstanding balance of any long-term debt used for acquisition, construction or improvement of those assets and increased by unspent proceeds. Net assets are reported as restricted when there are limitations imposed on their use through external restrictions imposed by creditors, grantors or laws or regulations of other governments.

G. Income Taxes

The Electric Utility is exempt from federal and state income taxes because it is a governmental entity organized under the provisions of Chapter 388 of the Code of Iowa.

H. Revenues and Unbilled Usage

Revenues are based on billing rates, which are applied to customers' consumption of electricity. The Utility records estimated unbilled revenue at the end of accounting periods. Revenues earned, but not yet billed at December 31, 2010 and 2009, totaled \$470,381 and \$433,242, respectively.

I. Estimates

The preparation of the financial statements in conformity in U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results may differ from those estimates.

Note 2 - CASH AND CASH EQUIVALENTS AND NONCURRENT INVESTMENTS

The Utility's deposits in Banks at December 31, 2010 and 2009 were entirely covered by federal depository insurance or by the State Sinking Fund in accordance with Chapter 12C of the Code of Iowa. This chapter provides for additional assessments against the depositories to insure there will be no loss of public funds.

**MUNICIPAL ELECTRIC UTILITY
OF THE CITY OF SPENCER, IOWA
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2010 AND 2009**

Note 2 - CASH AND CASH EQUIVALENTS AND NONCURRENT INVESTMENTS (Continued)

The Utility is authorized by statute and Board of Trustees' approval to invest public funds in obligations of the United States government, its agencies, and instrumentalities; certificates of deposit and other evidences of deposit at federally insured Iowa depository institutions; and the Iowa Public Agency Investment Trust.

The Utility had investments in Iowa Public Agency Investment Trust which are valued at an amortized cost of \$0 in pursuant to Rule 2a-7 under the Investment Company Act of 1940.

Interest Rate Risk – The Utility's investment policy limits the investment of operating funds (funds expected to be expended in the current budget year or within 15 months of receipt) in instruments that mature within 397 days. Funds not identified as operating funds may be invested in investments with maturities longer than 397 days, but the maturities shall be consistent with the needs and use of the Utility.

Credit Risk – The Utility's investment in the Iowa Public Agency Investment Trust is unrated. The remaining investments consisted of Certificate of Deposits are protected per Chapter 12C of the Iowa Code, and credit risk and concentration risks do not apply.

The Utility considers all highly liquid investments with an original maturity of three months or less to be cash equivalents for purposes of the statement of cash flows.

Investments are recorded at cost which approximates market. Adjustments are made to cost for any premium or discount, which is amortized over the maturity of the investment. Adjustments are also made to account for the change in accrued interest on respective investments.

Reconciliation of the Utility's cash and cash equivalents and noncurrent investments is as follows:

	<u>2010</u>	<u>2009</u>
Cash and cash equivalents:		
Board designated	\$ 4,000,000	\$ -
Consumer Deposits	74,711	59,036
Restricted	110,936	79,630
Unrestricted	828,811	681,449
Total cash and cash equivalents	5,014,458	820,115
Noncurrent investments:		
Unrestricted	-	62,848
Board designated	4,500,000	8,500,000
Restricted	2,308,455	2,310,213
Total noncurrent investments	6,808,455	10,873,061
Total cash and cash equivalents and noncurrent investments	<u>\$11,822,913</u>	<u>\$11,693,176</u>

**MUNICIPAL ELECTRIC UTILITY
OF THE CITY OF SPENCER, IOWA
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2010 AND 2009**

Note 3 - BOARD DESIGNATED FUNDS

The Board of Trustees of the Utility has designated certain funds to be placed in a contingency reserve account. These funds, which are from unrestricted net assets, are being designated for contingencies such as a natural disaster, and cannot be expended without Board approval.

The Board of Trustees of the Utility has designated certain funds to be placed in a replacement and construction reserve account. These funds, which are from unrestricted net assets, are being designated for replacement of property, plant and equipment and for new construction. These funds cannot be expended without Board approval.

Assets of the funds as of December 31, 2010 are summarized as follows:

	Contingency Reserve	Replacement and Construction Reserve	Total
Cash and cash equivalents	\$ -	\$ 4,000,000	\$ 4,000,000
Noncurrent investments	-	4,500,000	4,500,000
Total	\$ -	\$ 8,500,000	\$ 8,500,000

Assets of the funds as of December 31, 2009 are summarized as follows:

	Contingency Reserve	Replacement and Construction Reserve	Total
Noncurrent investments	\$ -	\$ 8,500,000	\$ 8,500,000

**MUNICIPAL ELECTRIC UTILITY
OF THE CITY OF SPENCER, IOWA
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2010 AND 2009**

Note 4 - CAPITAL ASSETS

Capital assets activity for the year ended December 31, 2010 was as follows:

	Beginning Balance	Additions and Transfers In	Deletions and Transfers Out	Ending Balance
Capital assets not being depreciated:				
Land	\$ 86,092	\$ 37,512	\$ -	\$ 123,604
Construction in progress	554,345	584,216	(66,836)	1,071,725
Total capital assets not being depreciated	640,437	621,728	(66,836)	1,195,329
Capital assets being depreciated:				
Infrastructure	64,414,386	223,984	(50,997)	64,587,373
Buildings and improvements	706,775	22,100	-	728,875
Equipment	6,221,189	495,001	-	6,716,190
Total capital assets being depreciated	71,354,350	741,085	(50,997)	72,044,438
Less accumulated depreciation	33,572,633	2,423,956	(42,285)	35,954,304
Total capital assets being depreciated - net	37,781,717	(1,682,871)	(8,712)	36,090,134
Capital assets - net	\$38,422,154	\$(1,061,143)	\$(75,548)	\$37,285,463

**MUNICIPAL ELECTRIC UTILITY
OF THE CITY OF SPENCER, IOWA
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2010 AND 2009**

Note 4 - CAPITAL ASSETS (Continued)

Capital assets activity for the year ended December 31, 2009 was as follows:

	Beginning Balance	Deletions And Transfers In	Deletions and Transfers Out	Ending Balance
Capital assets not being depreciated:				
Land	\$ 86,092	\$ -	\$ -	\$ 86,092
Construction in progress	1,019,179	156,255	(621,089)	554,345
Total capital assets not being depreciated	1,105,271	156,255	(621,089)	640,437
Capital assets being depreciated:				
Infrastructure	63,090,546	1,467,352	(131,512)	64,414,386
Buildings and improvements	706,775	-	-	706,775
Equipment	5,917,907	397,127	(93,845)	6,221,189
Total capital assets being depreciated	69,715,228	1,864,479	(225,357)	71,354,350
Less accumulated depreciation	31,344,222	2,305,469	(77,058)	33,572,633
Total capital assets being depreciated - net	38,371,006	(440,990)	(148,299)	37,781,717
Capital assets – net	\$39,476,277	\$(284,735)	\$(769,388)	\$38,422,154

Spencer Municipal Utilities had invested approximately \$599,000 for the development and construction of Sutherland Generating Station Unit 4. During March 2009 Interstate Power and Light, an Alliant Energy Company, cancelled plans to construct the plant. A cash settlement was negotiated and Spencer Municipal Utilities received \$225,365 and recognized a loss of \$373,177.

Note 5 - NOTES RECEIVABLE – EMPLOYEES

The Board of trustees had authorized the Electric Utility to purchase personal computers for interested employees. The employees repay the Utility through payroll withholding over a maximum of 24 months. No interest is charged on the unpaid balance. The program ended in August 2009 when all balances were paid in full.

**MUNICIPAL ELECTRIC UTILITY
OF THE CITY OF SPENCER, IOWA
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2010 AND 2009**

Note 6 - TRANSFERS IN LIEU OF PROPERTY TAXES/NOTE RECEIVABLE

By resolution of the Board of Trustees, voluntary transfers in lieu of property taxes are made to the City of Spencer, Iowa. Currently, transfers approximate 5% of gross sales (excluding the energy cost adjustment), less actual property taxes paid (on the George Neal Generating Station Unit No. 4 and on the Walter Scott Jr. Unit No. 4) and returned to the City of Spencer, Iowa. Additionally, funds declared to be surplus can be, and have been, transferred to the City.

During 2007, the Utility loaned the City \$375,000 to fund the economic development loan to Shine Bros. Corp. The City reimburses the Utility in equal payments of \$2,083 without interest, payable monthly. The balance of this note at December 31, 2010 was \$287,500 and December 31, 2009 was \$312,500.

A loan agreement was executed on June 1, 2009 between Spencer Municipal Utilities and the City of Spencer. The City has the ability to borrow up to \$1,000,000 at 2.75% until the maturity date of December 1, 2010, at which time all principal and interest is due. The loan was for the purpose of covering the cost to construct street and sewer improvements at the Green Industrial Center site. As of December 2010, the loan was paid in full which was comprised of a \$630,000 principal payment and \$20,220.41 in accrued interest.

A loan agreement was effective on July 15, 2009 between Spencer Municipal Utilities and the City of Spencer. The City borrowed \$383,430 for the purposes of loaning to Spencer Industries Foundation, Inc. The funds were used to construct an industrial building. The City is to repay the loan the earlier of the sale or lease of the building or by July 15, 2019. Interest will not accrue on the loan until July 15, 2014 at a rate of 3%.

Note 7 - NOTE RECEIVABLE - MUNICIPAL COMMUNICATIONS UTILITY

The Board of Trustees has approved an \$8,000,000 line of credit for the Municipal Communications Utility for use in start-up and construction costs related to bringing the Communications Utility into operation. The balance of the line of credit at December 31, 2010 and 2009 was \$3,000,000. Outstanding balances bear interest at a rate of 4.5% per annum.

Note 8 - BONDS PAYABLE

Bonds payable activity for the year ended December 31, 2010 was as follows:

	Beginning Balance	Additions	Reductions	Ending Balance	Due within One Year
Series 2004 revenue bonds	\$4,605,000	\$ -	\$ -	\$4,605,000	\$ -
Series 2008 revenue bonds	3,970,000	-	595,000	3,375,000	620,000
Total revenue bonds	<u>\$8,575,000</u>	<u>\$ -</u>	<u>\$595,000</u>	<u>\$7,980,000</u>	<u>\$620,000</u>

During 2009, a principal payment in the amount of \$1,650,000 was paid on the 2004 revenue bonds. The next principal payment due on the 2004 bonds is December 1, 2013.

**MUNICIPAL ELECTRIC UTILITY
OF THE CITY OF SPENCER, IOWA
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2010 AND 2009**

Note 8 – BONDS PAYABLE (Continued)

The Series 2004 and 2008 revenue bonds require annual principal payments, due December 1, and semiannual interest payments, due June 1 and December 1. Interest rates throughout the term of the bonds range between 1.4% and 4.6 %. The bonds are secured by the future net revenues of the Utility. Long-term debt matures and bears interest as follows:

Year	Series 2008		Series 2004		Total
	Principal	Interest	Principal	Interest	
2011	\$ 620,000	\$ 147,763	\$ -	\$ 187,478	\$ 955,241
2012	645,000	121,412	-	187,478	953,890
2013	670,000	94,000	585,000	187,478	1,536,478
2014	700,000	65,190	605,000	166,418	1,536,608
2015	740,000	34,040	630,000	143,730	1,547,770
2016-2019	-	-	2,785,000	306,485	3,091,485
Total	\$ 3,375,000	\$ 462,405	\$ 4,605,000	\$ 1,179,067	\$ 9,621,472

The bond resolutions provide certain covenants relating to the collection, segregation, and distribution of revenues from customers; places certain restrictions on future borrowing and leasing or disposition of assets; and requires that minimum insurance coverage be maintained.

Revenue Bonds

The Utility has pledged future utility revenue, net of specified operating expenses, to repay outstanding utility revenue bonds. The bonds are payable solely from the utility's net revenues and are payable through 2019. The total principal and interest remaining to be paid on the bonds is \$9,621,472. Principal and interest due for the current year and total combined utilities net revenues were \$955,528 and \$412,976, respectively.

Restricted Funds

Outstanding Electric Revenue Bonds are collateralized by the revenue of the Utility and the various special funds established by bond covenants. The covenants provide that the revenue of the Utility is to be used first to pay operating and maintenance expenses of the system and second to establish and maintain the special funds. Remaining revenues may then be used for any lawful purpose. The covenants also contain provisions which, among other items, restrict the issuance of additional revenue bonds unless the special funds noted above contain the required amounts and certain financial ratios are met. As of December 31, 2010 the Utility is in compliance with all bond covenant requirements.

**MUNICIPAL ELECTRIC UTILITY
OF THE CITY OF SPENCER, IOWA
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2010 AND 2009**

Note 8 – BONDS PAYABLE (Continued)

At December 31, 2010, the special funds consisted of the following:

	Cash and Cash Equivalents	Noncurrent Investments	Total
Bond Sinking Fund	\$ 79,642	\$ -	\$ 79,642
Bond Reserve Fund	-	1,558,039	1,558,039
Bond Improvement Fund	-	750,416	750,416
Total Restricted Net Assets	\$ 79,642	\$ 2,308,455	\$ 2,388,097

At December 31, 2009, the special funds consisted of the following:

	Cash and Cash Equivalents	Noncurrent Investments	Total
Bond Sinking Fund	\$ 79,630	\$ -	\$ 79,630
Bond Reserve Fund	-	1,559,797	1,559,797
Bond Improvement Fund	-	750,416	750,416
Total Restricted Net Assets	\$ 79,630	\$ 2,310,213	\$ 2,389,843

Monthly deposits into two bond sinking funds are required to establish the amount necessary to pay the next installments of principal and interest on the 2004 and 2008 Electric Revenue Bonds. Bond reserve funds for the 2004 and 2008 Electric Revenue Bonds equaled the required balance at December 31, 2010 and 2009; therefore monthly deposits into the fund are not currently required. These funds may be used to pay principal and interest payments when insufficient funds are available in the sinking fund.

The bond improvement fund balance at December 31, 2010 and 2009 equaled the minimum balance required; therefore monthly deposits into the fund are not currently required. These funds are to be used first for principal and interest payments when insufficient funds are available in the sinking and reserve funds and second for extraordinary unbudgeted maintenance expenses or system repairs, renewals and replacements.

Note 9 - RATE MATTERS

Rates of the Utility are established by the Board of Trustees and, as a municipal system, are not subject to the regulation of the Utilities Division of the Department of Commerce of the State of Iowa.

Note 10 - NUMBER OF METER CONNECTIONS

The number of meter connections totaled 6,084 and 6,073 at December 31, 2010 and 2009, respectively.

**MUNICIPAL ELECTRIC UTILITY
OF THE CITY OF SPENCER, IOWA
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2010 AND 2009**

Note 11 - LEASES

The Utility leases electrical generation capacity of a jet turbine generator, its share of the Neal 4 plant, its share of the Wisdom 2 plant, and its share of the Walter Scott 4 plant under operating leases to other utilities or their associations. The revenues from such leases are classified as leased facilities. The Utility's investment in these facilities is included in capital assets in service and is set forth as follows:

	<u>2010</u>	<u>2009</u>
Jet turbine generator	\$ 2,537,488	\$ 2,537,488
Neal 4 plant	4,875,630	4,883,410
Wisdom 2 plant	2,314,530	2,314,530
Walter Scott 4 plant	14,666,778	14,627,555
Total	<u>24,394,426</u>	<u>24,362,983</u>
Less accumulated depreciation	<u>8,240,619</u>	<u>7,570,782</u>
Net investment	<u>\$16,153,807</u>	<u>\$16,792,201</u>

The lease of the Neal 4, Walter Scott 4 and Wisdom 2 plant are long-term commitments based on capacity. The amount is determined by formula based on usage and totaled \$13,162, \$1,017,588 and \$174,640, respectively, in 2010. The leases of the jet turbine generator are both by non-cancelable lease and a variable lease determined by capacity and totaled \$99,008 in 2010 and \$141,962 in 2009. The following is a schedule of future minimum rentals on non-cancelable operating leases on the jet turbine generator as of December 31, 2010:

2011	\$ 65,000
2012	65,000
2013	65,000
2014	65,000
2015	<u>120,000</u>
Total minimum lease payment receivable	<u>\$ 380,000</u>

The Utility leases bandwidth, property, and building space to the Water Utility and Communications Utility. The revenues from such leases are classified as leased facilities and totaled \$432,871 and \$431,718 in 2010 and 2009, respectively. The leases are 20-year variable leases based on bandwidth and space utilized. The payable at December 31, 2010 and 2009 was \$413,511 and \$412,358, respectively.

The Utility leases building space from the Water Utility. The expense from the lease is classified as operating expense. The lease is a monthly lease based on building space utilized and totaled \$9,600 in 2010 and 2009. The payable at December 31, 2010 and 2009 was \$9,600.

**MUNICIPAL ELECTRIC UTILITY
OF THE CITY OF SPENCER, IOWA
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2010 AND 2009**

Note 12 - RETIREMENT SYSTEM

IPERS

The Utility contributes to the Iowa Public Employees Retirement System (IPERS) which is a cost-sharing multiple-employer defined benefit pension plan administered by the State of Iowa. IPERS provides retirement and death benefits which are established by state statute to plan members and beneficiaries. IPERS issues a publicly available financial report that includes financial statements and required supplementary information. The report may be obtained by writing to IPERS, PO Box 9117, Des Moines, Iowa, 50306-9117.

Plan members were required to contribute 4.30% through June 30, 2010 and 4.45% presently of their annual salary and the Utility was required to contribute 6.65% through June 30, 2010 and 6.95% presently of annual payroll. Contribution requirements are established by State statute. The Utility's contributions to IPERS for the years ended December 31, 2010, 2009 and 2008 were \$118,799, \$111,230 and \$108,221, respectively, equal to the required contributions for the year.

Employees Pension Plan

All full-time employees of the Electric Utility who have completed six months of continuous employment and are 18 years of age are eligible to participate in a 457b Pension Plan administered by Security National Bank. The Utility contributes 8% of the employees' compensation for all employees contributing at least 2% of their salary.

The Electric Utility's contribution to the 457b Pension Plan for 2010 and 2009 totaled \$138,560 and \$135,185, respectively.

Note 13 - OTHER POST EMPLOYMENT BENEFITS

During fiscal 2008, the Utility adopted the provisions of GASB 45 "Accounting and Financial Reporting by Employers for Post-Employment Benefits Other Than Pensions". The major change under GASB 45 is to attribute the cost of post-employment benefits to the time during which the employee is working for the employer. Accordingly, a prospective liability is recorded at June 30, 2010 for a Post-Employment Benefit Obligation as determined by an actuarial calculation.

Plan Description. The Utility operates a single-employer retiree benefit plan which provides medical/prescription drug benefits for retirees and their family.

The medical/prescription drug coverage is provided through a fully-insured plan. Retirees under age 65 pay the same premium for the medical/prescription drug benefit as active employees, which results in a implicit subsidy and an OPEB liability.

Funding Policy. The Utility currently finances the retiree benefit plan on a pay-as-you-go basis.

**MUNICIPAL ELECTRIC UTILITY
OF THE CITY OF SPENCER, IOWA
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2010 AND 2009**

Note 13 – OTHER POST EMPLOYMENT BENEFITS (Continued)

Annual OPEB Cost and NET OPEB Obligation. The Utility's annual other post-employment benefit (OPEB) cost is calculated based on the annual required contribution of the employer (ARC), an amount actuarially determined in accordance with the parameters of GASB 45. The ARC represents a level of funding that, if paid on an ongoing basis, is projected to cover normal cost each year and amortize any unfunded actuarial liabilities over a period not to exceed thirty years.

The following table shows the components of the Utility's annual OPEB for the year, the amount actually contributed to the plan, and changes in the Utility's net OPEB obligation to the plan:

	<u>2010</u>	<u>2009</u>
Annual required contribution	\$ 16,514	\$ 14,975
Interest on net OPEB obligation	774	399
Adjustment to annual required contribution	<u>(771)</u>	<u>(577)</u>
Annual OPEB cost (Expense)	16,517	14,797
Contributions made	<u>(5,939)</u>	<u>(5,401)</u>
Increase in net OPEB obligation	10,578	9,396
Net OPEB obligation - beginning of year	<u>19,370</u>	<u>9,974</u>
Net OPEB obligation - end of year	<u><u>\$ 29,948</u></u>	<u><u>\$ 19,370</u></u>

The Utility's annual OPEB cost, the percentage of annual OPEB cost contributed to the plan, and the net OPEB obligation were as follows:

Fiscal Year Ended	Annual OPEB Cost	Percentage of Annual OPEB Cost Contributed	Net OPEB Obligation
2010	\$ 16,517	36.0%	\$ 29,948
2009	\$ 14,797	36.5%	\$ 19,370

Funded Status and Funding Progress. The funded status of the plan as of December 31, 2010 was as follows:

	<u>2010</u>	<u>2009</u>
Actuarial accrued liability (AAL)	\$160,019	\$142,863
Actuarial value of plan assets	<u>-</u>	<u>-</u>
Unfunded actuarial accrued liability (UAAL)	\$160,019	\$142,863
Covered payroll (active members)	\$1,749,265	\$1,698,615
UAAL as a percentage of covered payroll	9.1%	8.4%

**MUNICIPAL ELECTRIC UTILITY
OF THE CITY OF SPENCER, IOWA
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2010 AND 2009**

Note 13 – OTHER POST EMPLOYMENT BENEFITS (Continued)

Actuarial Methods and Assumptions. Actuarial valuations of an ongoing plan involve estimates of the value of reported amounts and assumptions about the probability of occurrence of events far into the future. Examples include assumptions about future employment, mortality, and the healthcare cost trend. Amounts determined regarding the funded status of the plan and the annual required contributions of the employer are subject to continual revision as actual results are compared with past expectations and new estimates are made about the future. The schedule of funding progress, presented as required supplementary information following the notes to the financial statements, presents multiyear trend information about whether the actuarial value of plan assets is increasing or decreasing over time relative to the actuarial accrued liabilities for benefits.

Projections of benefits for financial reporting purposes are based on the substantive plan and include the types of benefits provided at the time of each valuation and the historical pattern of sharing of benefit costs between the employer and plan members to that point and do not explicitly reflect the potential effect of legal or contractual funding limitation. The actuarial methods and assumptions used include techniques that are designed to reduce the effect of short-term volatility in actuarial accrued liabilities and the actuarial value of assets, consistent with the long-term perspective of the calculations.

In the December 31, 2010 actuarial valuation, the projected unit credit actuarial cost method was used. The actuarial assumptions included a 4% interest discount rate. The projected annual medical trend rate is 9%. The ultimate medical trend rate is 4.5%. The medical trend rate is reduced 0.5% each year until reaching the 4.5% ultimate trend rate.

Mortality rates are from the RP-2000 Combined Mortality Table projected to 2010 using Scale AA. The salary increase rate was assumed to be 3% per year. The UAAL is being amortized as a level dollar amount on an open basis over 30 years.

Note 14 - RISK MANAGEMENT

The Electric Utility is exposed to various risks of loss related to torts; theft, damage to and destruction of assets; errors and omissions; injuries to employees; and natural disasters. These risks are covered by the purchase of commercial insurance. The Utility assumes liability for any deductible and claims in excess of coverage limits. Settled claims from these risks have not exceeded commercial insurance coverage in any of the past three fiscal years. The Utility, as is typical in the electric power industry, does not insure its transmission or distribution lines due to the high cost of such coverage.

**MUNICIPAL ELECTRIC UTILITY
OF THE CITY OF SPENCER, IOWA
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2010 AND 2009**

Note 15 - RELATED PARTIES

The Electric Utility, Water Utility and Communications Utility of the City of Spencer, Iowa exchange services in the normal course of business.

Two members of the Board of Trustees hold non-controlling interests in a financial institution where the Utility maintains cash balances.

Additional related party items are included in Notes 7 and 11.

Note 16 - COMMITMENTS

Beginning in 2009, the Electric Utility pledged support to the Iowa Great Lakes Corridor of Opportunity at a level of \$25,000 per year for four years. This commitment is subject to annual review by the Utility Board

In May 2010 Spencer Municipal Utilities agreed to replace high pressure sodium light fixtures with new energy efficient LED streetlight fixtures. SMU will begin work in 2011 and will receive reimbursement in the amount of \$52,084 from the City of Spencer through a State Energy Grant from the Office of Energy Independence.

In October 2010 Spencer Municipal Utilities entered into a contract with Midstates Builders, Inc. The contract entails removal and replacement of the damaged portion of the 520 2nd Ave East building roof; provide new foundation, building frames and structures as needed. The contract amount is \$555,457 with project completion scheduled for September 2011.

Note 17 – SUBSEQUENT EVENT

In February 9, 2011 Board Meeting a 10% rate increase was approved for the following Utility rates: RE, GS, SCI, LCI, GS1 and GS4. The new rates will be calculated on consumption effective April 1, 2011 and will generate approximately an additional \$635,000 in revenue.

**MUNICIPAL ELECTRIC UTILITY
OF THE CITY OF SPENCER, IOWA
BUDGETARY COMPARISON SCHEDULE OF RECEIPTS, DISBURSEMENTS
AND CHANGES IN NET ASSETS - BUDGET AND ACTUAL (CASH BASIS)
REQUIRED SUPPLEMENTARY INFORMATION
FOR YEAR ENDED DECEMBER 31, 2010**

	Budgeted	Actual	Final to Actual Variance
Receipts:			
Municipal Electric Utility		\$ 12,585,348	
Municipal Water Utility		1,410,463	
Municipal Communications Utility		7,612,073	
Total Receipts	\$ 24,186,800	21,607,884	\$ (2,578,916)
Expenditures:			
Municipal Electric Utility		13,000,336	
Municipal Water Utility		1,676,865	
Municipal Communications Utility		5,976,879	
Total Expenditures	23,228,800	20,654,080	2,574,720
Excess (Deficiency) of Revenues Over Expenditures	958,000	953,804	(4,196)
Other Financing Sources (Uses); Transfers Out	(2,600,000)	-	2,600,000
Net Change in Net Assets	(1,642,000)	953,804	2,595,804
Net Assets at Beginning of Year	17,684,388	17,684,388	-
Net Assets at End of Year	\$ 16,042,388	\$ 18,638,192	\$ 2,595,804

**MUNICIPAL ELECTRIC UTILITY
OF THE CITY OF SPENCER, IOWA
BUDGET TO GAAP RECONCILIATION
REQUIRED SUPPLEMENTARY INFORMATION
FOR YEAR ENDED DECEMBER 31, 2010**

	Cash Basis	Accrual Adjustments	Accrual Basis
Receipts:			
Municipal Electric Utility	\$ 12,585,348	\$ 207,810	\$ 12,793,158
Municipal Water Utility	1,410,463	154,321	1,564,784
Municipal Communications Utility	7,612,073	(1,890,260)	5,721,813
Total Receipts	<u>21,607,884</u>	<u>(1,528,129)</u>	<u>20,079,755</u>
Expenditures:			
Municipal Electric Utility	13,000,336	1,268,271	14,268,607
Municipal Water Utility	1,676,865	(118,211)	1,558,654
Municipal Communications Utility	5,976,879	891,731	6,868,610
Total Expenditures	<u>20,654,080</u>	<u>2,041,791</u>	<u>22,695,871</u>
 Net Change in Net Assets	 953,804	 (3,569,920)	 (2,616,116)
 Net Assets at Beginning of Year	 <u>17,684,388</u>	 <u>45,995,135</u>	 <u>63,679,523</u>
 Net Assets at End of Year	 <u><u>\$ 18,638,192</u></u>	 <u><u>\$ 42,425,215</u></u>	 <u><u>\$ 61,063,407</u></u>

**MUNICIPAL ELECTRIC UTILITY
OF THE CITY OF SPENCER, IOWA
NOTES TO REQUIRED SUPPLEMENTARY INFORMATION –
BUDGETARY REPORTING
YEAR ENDED DECEMBER 31, 2010**

The budgetary comparison is presented as Required Supplementary Information in accordance with Government Accounting Standards Board Statement No. 41 for governments with significant budgetary perspective differences resulting from not being able to present budgetary comparisons for each individual utility.

In accordance with the Code of Iowa, Spencer Municipal Utilities annually adopts a combined budget on the cash basis for the Municipal Electric Utility, Municipal Water Utility, and Municipal Communications Utility of the City of Spencer, Iowa following required public notice and hearing. The annual budget may be amended during the year utilizing similar statutorily prescribed procedures. Encumbrances are not recognized and appropriations lapse at year-end.

**MUNICIPAL ELECTRIC UTILITY
OF THE CITY OF SPENCER, IOWA
FUNDING PROGRESS FOR THE RETIREE HEALTH PLAN
FOR YEAR ENDED DECEMBER 31, 2010**

Year Ended December 31,	Actuarial Valuation Date	Actuarial Value of Assets (a)	Actuarial Accrued Liability (AAL) (b)	Unfunded AAL (UAAL) (b-a)	Funded Ratio (a/b)	Covered Payroll (c)	UAAL as a Percentage of Covered Payroll ((b-a)/c)
2008	12/31/2008	\$ -	\$ 133,585	\$ 133,585	0%	\$ 1,648,850	8.1%
2009	12/31/2009	\$ -	\$ 142,863	\$ 142,863	0%	\$ 1,698,315	8.4%
2010	12/31/2010	\$ -	\$ 160,019	\$ 160,019	0%	\$ 1,749,265	9.1%

See Note 13 to the accompanying Notes to Financial Statements for the plan description, funding policy, annual OPEB Cost and Net OPEB Obligation, and the funded status and funding progress.

**INDEPENDENT AUDITORS' REPORT ON INTERNAL CONTROL OVER
FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS
BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN
ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS**

To the Board of Trustees
Spencer Municipal Utilities – Municipal Electric Utility
Spencer, Iowa 51301

We have audited the accompanying financial statements of Municipal Electric Utility of the City of Spencer, Iowa (Spencer Municipal Utility) as of and for the year ended December 31, 2010, which collectively comprise the Utility's basic financial statements listed in the table of contents, and have issued our report thereon dated April 5, 2011. We conducted our audit in accordance with U.S. generally accepted auditing standards and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered Spencer Municipal Utility's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing our opinion on the effectiveness of Spencer Municipal Utility's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of Spencer Municipal Utility's internal control over financial reporting.

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and would not necessarily identify all deficiencies in internal control over financial reporting that might be significant deficiencies or material weaknesses. However, as discussed below, we identified a certain deficiency in internal control over financial reporting that we consider to be a material weakness.

A deficiency in internal control exists when the design or operation of the control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect and correct misstatements on a timely basis. A material weakness is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility a material misstatement of the Utility's financial statements will not be prevented or detected and corrected on a timely basis. We consider the deficiency in internal control described in Part II of the accompanying Schedule of Findings as item II-A-10 to be a material weakness in internal control over financial reporting.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether Spencer Municipal Utility's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grants, non-compliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of non-compliance or other matters that are required to be reported under *Government Auditing Standards*.

Spencer Municipal Utility's responses to findings identified in our audit are described in the accompanying Schedule of Findings and Questioned Costs. While we have expressed our conclusions on the Utility's responses, we did not audit Spencer Municipal Utility's responses, and accordingly, we express no opinion on them.

This report, a public record by law, is intended solely for the information and use of the officials, employees and citizens of Spencer Municipal Utility and other parties to whom Spencer Municipal Utility may report, including federal awarding agencies and pass-through entities. This report is not intended to be and should not be used by anyone other than these specified parties.

We would like to acknowledge the many courtesies and assistance extended to us by personnel of Spencer Municipal Utility during the course of our audit. Should you have any questions concerning any of the above matters, we shall be pleased to discuss them with you at your convenience.

Williams + Company, P.C.
Certified Public Accountants

Spencer, Iowa
April 5, 2011

**SPENCER MUNICIPAL UTILITIES
MUNICIPAL ELECTRIC UTILITY
SCHEDULE OF FINDINGS
YEAR ENDED DECEMBER 31, 2010**

Part I: Summary of the Independent Auditors' Results:

- (a) An unqualified opinion was issued on the financial statements.
- (b) A significant deficiency in internal control over financial reporting was disclosed by the audit of the financial statements and is considered to be a material weakness.
- (c) The audit did not disclose any noncompliance which is material to the financial statements.

Part II: Findings Related to the General Purpose Financial Statements

SIGNIFICANT DEFICIENCY:

II-A-10 Financial Reporting – During the audit, we identified a material cash deposit that was posted to the incorrect period resulting in an understatement of cash and an overstatement of accounts receivable. This adjustment was subsequently made by Spencer Municipal Utility to properly record the deposit in the financial statements.

Recommendation – Spencer Municipal Utility should implement procedures to ensure all accounts are properly identified, classified, and included in Spencer Municipal Utility's financial statements.

Response – We will revise our current procedures to ensure the proper amounts are recorded in the financial statements in the future.

Conclusion - Response accepted.

INSTANCES OF NONCOMPLIANCE:

No matters were reported.

**SPENCER MUNICIPAL UTILITIES
MUNICIPAL ELECTRIC UTILITY
SCHEDULE OF FINDINGS
YEAR ENDED DECEMBER 31, 2010**

Part III: Other Findings Related to Required Statutory Reporting

III-A-10 Certified Budget – Disbursements during the year ended December 31, 2010 did not exceed the amounts budgeted in the business type activities function.

III-B-10 Questionable Expenditures – No expenditures were noted which did not meet the requirements of public purpose as defined in an Attorney General's opinion dated April 25, 1979.

III-C-10 Travel Expenses – No expenditures of the Utility's money for travel expenses of spouses of Utility's officials or employees were noted.

III-D-10 Business Transactions – Business transactions between Utility and Utility officials and employees are detailed as follows:

<u>Name, Title and Business Connection</u>	<u>Transaction Description</u>	<u>Amount</u>
Tom Howe, Board Member Part owner of H & N Chevrolet	Maintenance & Repairs	\$1,322
Dave Hultgren, Board Member Owner, Northwest Equipment	Maintenance & Repairs	\$ 607

In accordance with Chapter 362.5(10) of the Code of Iowa, the transactions with the Board Member do not appear to represent conflicts of interest since total transactions with each were less than \$1,500 during the year.

III-E-10 Bond Coverage – Surety bond coverage of Spencer Municipal Utilities' officials and employees is in accordance with statutory provisions. The amount of coverage should be reviewed annually to insure that the coverage is adequate for current operations.

III-F-10 Board Minutes – No transactions were found that we believe should have been approved in the Board minutes but were not.

III-G-10 Revenue Bonds – As of December 31, 2010 the Utility is in compliance with all bond covenant requirements.

III-H-10 Deposits and Investments – No instances of non-compliance with the deposit and investment provisions of Chapter 12(B) and 12(c) of the Code of Iowa and the Utility's investment policy were noted.

SPENCER MUNICIPAL UTILITIES

**MUNICIPAL WATER UTILITY
OF THE CITY OF SPENCER, IOWA**

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INDEPENDENT AUDITORS' REPORT

Board of Trustees
Spencer Municipal Utilities – Municipal Water Utility
Spencer, IA 51301

We have audited the accompanying financial statements of the business-type activity of Municipal Water Utility of the City of Spencer, Iowa (the Utility), as of and for the year ended December 31, 2010, which collectively comprise the Utility's basic financial statements as listed in the table of contents. These financial statements are the responsibility of management. Our responsibility is to express an opinion on these financial statements based on our audit. The prior year comparative information has been derived from the Utility's 2009 financial statements and, in our report dated May 6, 2010, we expressed an unqualified opinion on the respective financial statements of the business-type activity.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatements. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the business-type activity of the Utility as of December 31, 2010 and the respective changes in financial position and cash flows for the year then ended, in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated April 5, 2011, on our consideration of the Utility's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards*, and should be considered in conjunction with this report in considering the results of our audit.

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis, budgetary comparison and funding progress for the retiree health plan information on pages 35 through 37 and pages 55 through 58 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Williams & Company P.C.
Certified Public Accountants

Spencer, Iowa
April 5, 2011

MANAGEMENT'S DISCUSSION AND ANALYSIS

The purpose of management's discussion and analysis (MD&A) is to provide the reader with an introduction to the financial statements. Our discussion and analysis of the Municipal Water Utility (Utility) of the City of Spencer, Iowa's financial performance provides an overview of the Utility's financial activities for the years ended December 31, 2010 and 2009.

The following information should be read in conjunction with the financial statements and the accompanying notes to the financial statements that follow this section.

2010 Financial Highlights

The Utility delivered approximately 395,372,000 gallons of water to its retail customers in 2010 compared to approximately 407,714,000 gallons in 2009.

The Utility's net assets increased by \$6,130 to \$6,794,548 as a result of operations for the year ended December 31, 2010.

Overview of the Financial Statements

The balance sheets include the Utility's assets and liabilities and provide information about the nature and amounts of investments in resources (assets) and the obligations to creditors (liabilities).

The statement of revenues, expenses and changes in net assets report all revenues and expenses incurred during the fiscal year.

The Statement of Cash Flows present cash receipts, cash disbursements, and net changes in cash resulting from operations, capital and related financing activities and investing activities.

The notes to the financial statements provide the required disclosures and other information that is necessary to give the reader a complete understanding of the data provided in the statements. The notes present information about the Utility's accounting policies, material risks, obligations, commitments, contingencies and subsequent events.

Condensed Financial Information

The following condensed financial information serves as the key financial data and indicators for management, monitoring, and planning.

Condensed Statements of Net Assets

	<u>2010</u>	<u>2009</u>
Current assets	\$1,522,064	\$1,638,805
Noncurrent assets	1,000,000	1,000,000
Capital assets, net of depr.	5,790,852	5,820,703
Deferred costs	<u>8,200</u>	<u>9,424</u>
Total assets	<u>\$8,321,116</u>	<u>\$8,468,932</u>
Current liabilities	\$ 641,568	\$ 723,514
Long-term debt	<u>885,000</u>	<u>957,000</u>
Total liabilities	<u>\$1,526,568</u>	<u>\$1,680,514</u>
Invested in capital assets, net of related debt	\$4,833,852	\$4,794,703
Restricted	170,206	168,804
Unrestricted	<u>1,790,490</u>	<u>1,824,911</u>
Total net assets	<u>6,794,548</u>	<u>6,788,418</u>
Total liabilities and net assets	<u>\$8,321,116</u>	<u>\$8,468,932</u>

Condensed Statements of Revenues, Expenses and Changes in Net Assets

Sales of water	\$1,490,529	\$1,171,820
Other	<u>8,253</u>	<u>9,405</u>
Total operating revenue	<u>1,498,782</u>	<u>1,181,225</u>
System operation & maintenance	928,155	1,110,514
Depreciation & amortization	401,414	377,127
Customer service & administration	<u>112,442</u>	<u>128,145</u>
Total operating expenses	<u>1,442,011</u>	<u>1,615,786</u>
Operating Income (loss)	56,771	(434,561)
Interest income	13,404	13,934
Interest expense	(37,634)	(38,697)
Other income (expense)	<u>(26,411)</u>	<u>75,353</u>
Total non-operating revenues	(50,641)	50,590
Change in net assets	6,130	(383,971)
Net assets, beginning of year	<u>6,788,418</u>	<u>7,172,389</u>
Net assets, end of year	<u>\$6,794,548</u>	<u>\$6,788,418</u>

Financial Analysis

The Utility's total assets decreased by approximately \$148,000.

The Utility's gross revenues increased by approximately \$318,000 or 27% due to the \$10 customer charge effective with June 2010 consumption.

Total operating expenses decreased by approximately \$174,000 due to decreased expenses related to nearing completion of meter replacement project, reduction of meter reading time and distribution maintenance.

Total operating income generated in 2010 was \$56,771 compared to \$434,561 loss in 2009.

Contributions in Aid of Construction totaled \$9,792 for the year ended December 31, 2010 compared to \$83,100 for the year ended December 31, 2009.

The Utility had a net profit of \$6,130 for the year ended December 31, 2010 compared to a net loss of \$383,971 for the year ended December 31, 2009.

Capital Assets and Debt Administration

Net capital assets decreased by approximately \$30,000 due to depreciation exceeding assets placed in service.

Economic Factors

During the year ended December 31, 2010, the Utility experienced a net profit of \$6,130. The rate adjustment effective with consumption beginning June 1, 2010 allowed the Utility sufficient coverage of operational and non-operational expenses. Management will continue to monitor the operations of the Utility in addition to projected capital expenditures and propose rate adjustments accordingly.

Contacting the Utility's Financial Management

This financial report is designed to present our citizens, customers, and creditors with a general overview of the Utility's finances and operating activities. If you have any questions or require additional information please contact the Finance Manager, 712 Grand Ave, PO Box 222, Spencer, Iowa 51301.

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**MUNICIPAL WATER UTILITY
OF THE CITY OF SPENCER, IOWA
STATEMENTS OF NET ASSETS
DECEMBER 31, 2010 AND 2009**

	2010	2009
ASSETS		
Current Assets:		
Cash and Cash Equivalents		
Unrestricted	\$ 146,480	\$ 414,284
Board Designated	719,106	719,106
Restricted	170,206	168,804
Accounts Receivable (Net of Allowance for Doubtful Accounts of \$2,000)	336,471	218,108
Unbilled Usage	69,993	43,827
Materials And Supplies Inventory	70,820	68,109
Prepayments and Other	8,988	6,567
Total Current Assets	1,522,064	1,638,805
Capital Assets:		
Plant in Service	12,412,628	12,144,799
Accumulated Depreciation	(6,984,043)	(6,582,629)
Net Plant in Service	5,428,585	5,562,170
Land	258,533	258,533
Construction in Progress	103,734	-
Total Capital Assets	5,790,852	5,820,703
Noncurrent Assets:		
Noncurrent Investments		
Board Designated	1,000,000	1,000,000
Unamortized Bond Issue Costs	8,200	9,424
Total Noncurrent Assets	1,008,200	1,009,424
Total Assets	\$ 8,321,116	\$ 8,468,932

See Accompanying Notes to Financial Statements

**MUNICIPAL WATER UTILITY
OF THE CITY OF SPENCER, IOWA
STATEMENTS OF NET ASSETS
DECEMBER 31, 2010 AND 2009**

	2010	2009
LIABILITIES AND NET ASSETS		
Current Liabilities:		
Accounts Payable	\$ 532,263	\$ 629,140
Payroll and Sales Tax Payable	9,580	1,449
Accrued Payroll and Compensated Absences	21,634	17,395
Accrued Interest Payable	6,091	6,530
Current Maturities of Long-Term Debt	72,000	69,000
Total Current Liabilities	<u>641,568</u>	<u>723,514</u>
Bonds Payable:		
Bonds Payable	957,000	1,026,000
Less - Current Maturities	(72,000)	(69,000)
Total Bonds Payable	<u>885,000</u>	<u>957,000</u>
Total Liabilities	<u>1,526,568</u>	<u>1,680,514</u>
Net Assets		
Invested in Capital Assets, Net of Related Debt	4,833,852	4,794,703
Restricted	170,206	168,804
Unrestricted	1,790,490	1,824,911
Total Net Assets	<u>\$ 6,794,548</u>	<u>\$ 6,788,418</u>

See Accompanying Notes to Financial Statements

**MUNICIPAL WATER UTILITY
OF THE CITY OF SPENCER, IOWA
STATEMENTS OF REVENUES, EXPENSES AND
CHANGES IN FUND NET ASSETS
FOR THE YEARS ENDED DECEMBER 31, 2010 AND 2009**

	2010	2009
Operating Revenues:		
Residential	\$ 1,050,837	\$ 797,072
Commercial	439,692	374,748
Service Permits	7,100	7,975
Miscellaneous	1,153	1,430
Total Operating Revenues	1,498,782	1,181,225
Operating Expenses:		
Treatment	434,154	407,490
Distribution	494,001	703,024
Depreciation and Amortization	401,414	377,127
Customer Operations	26,771	52,538
General and Administrative	85,671	75,607
Total Operating Expenses	1,442,011	1,615,786
Operating Income (Loss)	56,771	(434,561)
Non-Operating Income (Expense):		
Interest Income on Investments	13,404	13,934
Contributions From Developers	9,792	83,100
Resource Conservation	(19,069)	-
Leased Facilities	37,353	35,468
Interest Expense	(37,634)	(38,697)
Bond Amortization Expense	(1,224)	(1,224)
Inventory Sales	5,453	11,523
Gain on Plant Retirements	-	666
Payment in Lieu of Property Taxes	(58,716)	(54,180)
Total Non-Operating Income (Loss)	(50,641)	50,590
Change in Net Assets	6,130	(383,971)
Net Assets at Beginning of Year	6,788,418	7,172,389
Net Assets at End of Year	\$ 6,794,548	\$ 6,788,418

See Accompanying Notes to Financial Statements

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**MUNICIPAL WATER UTILITY
OF THE CITY OF SPENCER, IOWA
STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED DECEMBER 31, 2010 AND 2009**

	<u>2010</u>	<u>2009</u>
Cash Flows From Operating Activities:		
Cash Received From Customers	\$ 1,354,253	\$ 1,282,563
Cash Payments to Suppliers for Goods and Services	(683,645)	(678,905)
Cash Payments to Employees for Services	(446,591)	(430,930)
Cash Payments In Lieu of Property Taxes	(58,716)	(54,180)
Cash Payments for Resource Conservation	(19,069)	-
Payments Received From Leasing of Facilities	37,353	35,468
	<u>183,585</u>	<u>154,016</u>
Net Cash Provided By Operating Activities		
Cash Flows From Capital and Related Financing Activities:		
Acquisition & Construction of Property and Equipment	(361,771)	(460,635)
Proceeds from Sale of Capital Assets	-	666
Revenue Bond Principal Repayment	(69,000)	(66,000)
Payments Received From Sale of Inventory	5,453	11,523
Interest Paid	(38,073)	(37,953)
	<u>(463,391)</u>	<u>(552,399)</u>
Net Cash (Used) By Capital and Related Financing Activities		
Cash Flows From Investing Activities:		
Interest Received From Investments	13,404	13,934
	<u>13,404</u>	<u>13,934</u>
Net Cash Provided By Investing Activities		
Net (Decrease) in Cash	(266,402)	(384,449)
Cash and Cash Equivalents at Beginning of Year	1,302,194	1,686,643
Cash and Cash Equivalents at End of Year	<u>\$ 1,035,792</u>	<u>\$ 1,302,194</u>
Reconciliation:		
Cash and Cash Equivalents		
Unrestricted	\$ 146,480	\$ 414,284
Restricted	170,206	168,804
Board Designated	719,106	719,106
	<u>\$ 1,035,792</u>	<u>\$ 1,302,194</u>

See Accompanying Notes to Financial Statements

**MUNICIPAL WATER UTILITY
OF THE CITY OF SPENCER, IOWA
STATEMENTS OF CASH FLOWS (CONTINUED)
FOR THE YEARS ENDED DECEMBER 31, 2010 AND 2009**

	2010	2009
Reconciliation of Operating Income (Loss) to Net Cash Provided by Operating Activities		
Operating Income (Loss)	\$ 56,771	\$ (434,561)
Adjustments to Reconcile Operating Income (Loss) to Net Cash Provided By Operating Activities		
Depreciation and Amortization	401,414	377,127
Leased Facilities Income	37,353	35,468
Payment in Lieu of Property Taxes	(58,716)	(54,180)
Payment for Resource Conservation	(19,069)	-
(Increase) Decrease in Operating Assets:		
Accounts Receivable	(118,363)	87,597
Unbilled Usage	(26,166)	2,412
Materials and Supplies Inventory	(2,711)	11,329
Prepayments	(2,421)	1,202
Increase (Decrease) in Operating Liabilities:		
Accounts Payable	(96,877)	138,296
Accrued Payroll and Compensated Absences	12,370	(10,674)
Total Adjustments	126,814	588,577
Net Cash Provided By Operating Activities	\$ 183,585	\$ 154,016

See Accompanying Notes to Financial Statements

**MUNICIPAL WATER UTILITY
OF THE CITY OF SPENCER, IOWA
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2010 AND 2009**

Note 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

A. Organization and Basis of Accounting

The Municipal Water Utility of the City of Spencer, Iowa (Water Utility or Utility) operates as an independent unit of the City of Spencer and is managed, along with the Municipal Electric Utility and the Municipal Communication Utility of the City of Spencer, Iowa by a five member Board of Trustees.

The Utility follows the accounting practices prescribed through the Federal Energy Regulatory Commission for regulated utilities and proprietary fund accounting for governmental entities under accounting principles generally accepted in the United States of America.

For financial reporting purposes, the Utility has included all funds. The Utility has also considered all potential component units for which it is financially accountable, and other organizations for which the nature and significance of their relationship with the Utility are such that exclusion would cause the Utility's financial statements to be misleading or incomplete. The Governmental Accounting Standards Board has set forth criteria to be considered in determining financial accountability. These criteria include appointing a voting majority of an organization's governing body, and (1) the ability of the Utility to impose its will on that organization or (2) the potential for the organization to provide specific benefits to, or impose specific financial burdens on the Utility. It was determined that the Utility has no component units.

The Utility is not considered to be a component unit of the City of Spencer for financial statement purposes.

The Utility's financial statements are reported using the economic resources measurement focus and the accrual basis of accounting. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows.

In reporting the financial activity of its enterprise fund, the Utility applies all applicable GASB pronouncements as well as the following pronouncements issued on or before November 30, 1989, unless these pronouncements conflict with or contradict GASB pronouncements: Financial Accounting Standards Board Statements and Interpretations, Accounting Principles Board Opinions and Accounting Research Bulletins of the Committee on Accounting Procedure.

The Utility distinguishes operating revenues and expenses from non-operating items. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with the Utility's principal ongoing operations. The principal operating revenues of the Utility are charges to customers for sales and services. Operating expenses include the cost of sales and services, administrative expenses, and depreciation on capital assets. All revenues and expenses not meeting this definition are reported as non-operating revenues and expenses.

**MUNICIPAL WATER UTILITY
OF THE CITY OF SPENCER, IOWA
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2010 AND 2009**

Note 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

B. Capital Assets and Depreciation

Capital assets are stated at original cost when first devoted to public service. Currently, such costs include labor-related expenditures, such as payroll taxes, pensions, and other fringe benefits and administrative costs for labor related to the construction of new water facilities. In addition, net interest costs on construction debt are capitalized.

Replacements and betterments of capital assets are charged to capital assets. Routine maintenance and repairs are charged to expense as incurred.

Depreciation is provided on a straight-line basis. Current depreciation expense is approximately 2.84% of the original cost of depreciable water plant in service.

The estimated useful lives used to depreciate assets by class are as follows:

Infrastructure	40 years
Buildings and Equipment	5-20 years
Vehicles	5 years

C. Accounts Receivable

Accounts receivable are stated at the amount the Utility expects to collect from outstanding balances. The Utility provides for probable uncollectible amounts through a charge to earnings and a credit to a valuation allowance based on its assessment of the current status of individual accounts. Balances that are still outstanding after the Utility has used reasonable collection efforts are written off through a charge to the valuation allowance and a credit to accounts receivable. Changes in the valuation allowance have not been material to the financial statements.

D. Inventories

Inventories are valued at the lower of cost or market. The average cost method is used for determining the cost of materials and supplies inventory. Inventories are recorded as an expenditure or, if applicable, capitalized when consumed.

E. Unamortized Bond Issue Costs

Unamortized debt issue costs are amortized over the life of the debt on a straight line basis which approximates the effective interest method.

**MUNICIPAL WATER UTILITY
OF THE CITY OF SPENCER, IOWA
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2010 AND 2009**

Note 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

F. Net Assets

Net assets represent the difference between assets and liabilities in the financial statements. Net assets invested in capital assets, net of related debt, consists of capital assets, net of accumulated depreciation, reduced by the outstanding balance of any long-term debt used for acquisition, construction or improvement of those assets and increased by unspent debt when there are limitations imposed on their use through external restrictions imposed by creditors, grantors or laws or regulations of other governments.

The Utility's policy is to first apply restricted resources when an expense is incurred for purposes for which both restricted and unrestricted net assets are available.

G. Income Taxes

The Water Utility is exempt from federal and state income taxes because it is a governmental entity organized under the provisions of Chapter 388 of the Code of Iowa.

H. Revenues and Unbilled Usage

Revenues are based on billing rates, which are applied to customers' consumption of water. The Utility records estimated unbilled revenue at the end of accounting periods. Revenues earned, but not yet billed at December 31, 2010 and 2009, totaled \$69,993 and \$43,827, respectively.

I. Estimates

The preparation of the financial statements in conformity with U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results may differ from those estimates.

Note 2 - CASH AND CASH EQUIVALENTS AND NONCURRENT INVESTMENTS

The Utility's deposits in bank at December 31, 2010 and 2009 were entirely covered by federal depository insurance or by the State Sinking Fund in accordance with Chapter 12C of the Code of Iowa. This chapter provides for additional assessments against the depositories to insure there will be no loss of public funds.

The Utility is authorized by statute and Board of Trustees' approval to invest public funds in obligations of the United States government, its agencies and instrumentalities; certificates of deposit and other evidences of deposit at federally insured Iowa depository institutions; and the Iowa Public Agency Investment Trust.

The Utility had investments in Iowa Public Agency Investment Trust at December 31, 2010 and 2009 in the amount of \$1,407,154 and \$0, respectively, which was transferred to the operating checking account. The transfer was done in an effort to receive a higher rate of return and keep the same liquidity of funds that the Iowa Public Agency Investment Trust provided.

**MUNICIPAL WATER UTILITY
OF THE CITY OF SPENCER, IOWA
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2010 AND 2009**

Note 2 - CASH AND CASH EQUIVALENTS AND NONCURRENT INVESTMENTS (Continued)

Interest Rate Risk – The Utility’s investment policy limits the investment of operating funds (funds expected to be expended in the current budget year or within 15 months of receipt) in instruments that mature within 397 days. Funds not identified as operating funds may be invested in investments with maturities longer than 397 days, but the maturities shall be consistent with the needs and use of the Utility.

Credit Risk – The Utility’s investment in the Iowa Public Agency Investment Trust is unrated. The remaining investments consisted of Certificate of Deposits are protected per Chapter 12C of the Iowa Code, and credit risk and concentration risks do not apply.

The Utility considers all highly liquid investments with an original maturity of three months or less to be cash equivalents for purposes of the statement of cash flows.

Investments are recorded at cost which approximates market. Adjustments are made to cost for any premium or discount, which is amortized over the maturity of the investment. Adjustments are also made to account for the change in accrued interest on respective investments.

Reconciliation of the Utility’s cash and cash equivalents and noncurrent investments is as follows:

	<u>2010</u>	<u>2009</u>
Cash and cash equivalents:		
Board designated	\$ 719,106	\$ 719,106
Restricted	170,206	168,804
Unrestricted	146,480	414,284
Total cash and cash equivalents	<u>1,035,792</u>	<u>1,302,194</u>
Noncurrent investments:		
Board designated	1,000,000	1,000,000
Total noncurrent investments	<u>1,000,000</u>	<u>1,000,000</u>
Total cash and cash equivalents and noncurrent investments	<u>\$ 2,035,792</u>	<u>\$ 2,302,194</u>

**MUNICIPAL WATER UTILITY
OF THE CITY OF SPENCER, IOWA
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2010 AND 2009**

Note 3 - BOARD DESIGNATED FUNDS

The Board of trustees of the Utility has designated certain funds to be placed in a contingency reserve account. These funds, which are from unrestricted net assets, are being designated for contingencies such as a natural disaster and cannot be expended without Board approval.

The Board of Trustees of the Utility has designated certain funds to be placed in a replacement and construction reserve account. These funds, which are from unrestricted net assets, are being designated for replacement of property, plant, and equipment and for new construction. These funds cannot be expended without Board approval.

Assets of the funds as of December 31, 2010 are summarized as follows:

	Contingency Reserve	Replacement and Construction Reserve	Total
Cash and cash equivalents	\$ 469,106	\$ 250,000	\$ 719,106
Noncurrent investments	-	1,000,000	1,000,000
Total	<u>\$ 469,106</u>	<u>\$ 1,250,000</u>	<u>\$ 1,719,106</u>

Assets of the funds as of December 31, 2009 are summarized as follows:

	Contingency Reserve	Replacement and Construction Reserve	Total
Cash and cash equivalents	\$ 469,106	\$ 250,000	\$ 719,106
Noncurrent investments	-	1,000,000	1,000,000
Total	<u>\$ 469,106</u>	<u>\$ 1,250,000</u>	<u>\$ 1,719,106</u>

**MUNICIPAL WATER UTILITY
OF THE CITY OF SPENCER, IOWA
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2010 AND 2009**

Note 4 - CAPITAL ASSETS

Capital assets activity for the year ended December 31, 2010 was as follows:

	Beginning Balance	Additions and Transfers In	Deletions and Transfers Out	Ending Balance
Capital assets not being depreciated:				
Land	\$ 258,533	\$ -	\$ -	\$ 258,533
Construction in progress	-	103,734	-	103,734
Total capital assets not being depreciated	258,533	103,734	-	362,420
Capital assets being depreciated:				
Infrastructure	7,590,259	207,049	-	7,797,308
Buildings and equipment	4,346,311	60,780	-	4,407,091
Vehicles	208,229	-	-	208,229
Total capital assets being depreciated	12,144,799	267,829	-	12,412,628
Less accumulated depreciation	6,582,629	401,414	-	6,984,043
Total capital assets being depreciated - net	5,562,170	(133,586)	-	5,428,585
Capital assets - net	\$ 5,820,703	\$ (29,852)	\$ -	\$ 5,790,852

Capital assets activity for the year ended December 31, 2009 was as follows:

	Beginning Balance	Additions and Transfers In	Deletions and Transfers Out	Ending Balance
Capital assets not being depreciated:				
Land	\$ 258,533	\$ -	\$ -	\$ 258,533
Construction in progress	2,320	2,300	(4,620)	-
Total capital assets not being depreciated	260,853	2,300	(4,620)	258,533
Capital assets being depreciated:				
Infrastructure	7,145,067	445,192	-	7,590,259
Buildings and equipment	4,273,897	83,334	(10,920)	4,346,311
Vehicles	183,722	25,782	(1,275)	208,229
Total capital assets being depreciated	11,602,686	554,308	(12,195)	12,144,799
Less accumulated depreciation	6,206,732	377,127	(1,230)	6,582,629
Total capital assets being depreciated - net	5,395,954	177,181	(10,965)	5,562,170
Capital assets - net	\$ 5,656,807	\$ 179,481	\$ (15,585)	\$ 5,820,703

**MUNICIPAL WATER UTILITY
OF THE CITY OF SPENCER, IOWA
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2010 AND 2009**

Note 5 - SEWER, STORM WATER, AND SOLID WASTE

The Electric Utility bills and collects sewer, storm water, and solid waste revenues for the City of Spencer. The resulting receivable and corresponding payable are recorded under the Water Utility. The City of Spencer reimburses the Electric Utility for these services.

Note 6 - TRANSFERS IN LIEU OF PROPERTY TAXES

By resolution of the Board of Trustees, voluntary transfers in lieu of property taxes are made to the City of Spencer, Iowa. Currently, transfers approximate 5% of gross sales. Additionally, funds declared to be surplus can be, and have been, transferred to the City.

Note 7 – BONDS PAYABLE

Bonds payable activity for the year ended December 31, 2010 was as follows:

	Beginning Balance	Additions	Reductions	Ending Balance	Amounts Due Within One Year
Series 2000 revenue bonds	\$1,026,000	\$ -	\$ 69,000	\$957,000	\$ 72,000

Bonds payable activity for the year ended December 31, 2009 was as follows:

	Beginning Balance	Additions	Reductions	Ending Balance	Amounts Due Within One Year
Series 2000 revenue bonds	\$1,092,000	\$ -	\$ 66,000	\$1,026,000	\$ 69,000

The Series 2000 revenue bonds require annual principal payments, due December 1, and semiannual interest payments, due June 1 and December 1. Interest rate through 5/1/2011 is 3.84% and effective 5/1/2011 throughout the term of the bonds is 3.00%. The bonds are secured by the future net revenues of the Utility. Long-term debt matures and bears interest as follows:

	Series 2000		
	Principal	Interest	Total
2011	\$ 72,000	\$ 31,649	\$ 103,649
2012	74,000	25,440	99,440
2013	77,000	23,175	100,175
2014	80,000	20,820	100,820
2015	83,000	18,375	101,375
2016-2020	467,000	51,735	518,735
2021	104,000	1,560	105,560
Total	\$ 957,000	\$ 172,754	\$ 1,129,754

**MUNICIPAL WATER UTILITY
OF THE CITY OF SPENCER, IOWA
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2010 AND 2009**

Note 7 – BONDS PAYABLE (Continued)

The bond resolutions provide certain covenants relating to the collection, segregation, and distribution of revenues from customers; places certain restrictions on future borrowing and leasing or disposition of assets; and requires that minimum insurance coverage be maintained.

Revenue Bonds

The Utility has pledged future utility revenue, net of specified operating expenses, to repay outstanding utility revenue bonds. The bonds are payable solely from the utility's net revenues and are payable through 2021. The total principal and interest remaining to be paid on the bonds is \$1,129,754. Principal and interest paid for the current year and total combined utilities net revenues were \$107,074 and 458,185, respectively.

Restricted Funds

Outstanding Water Revenue Bonds are collateralized by the revenue of the Utility and the various special funds established by bond covenants. The covenants provide that the revenue of the Utility is to be used first to pay operating and maintenance expenses of the system and second to establish and maintain the special funds. Remaining revenues may then be used for any lawful purpose. The covenants also contain provisions which, among other items, restrict the issuance of additional revenue bonds unless the special funds noted above contain the required amounts and certain financial ratios are met. As of December 31, 2010 and 2009 the Utility is in compliance with all bond covenant requirements except the Net Revenue requirement.

The special funds consisted of the following:

	2010	2009
Bond Sinking Fund	\$ 55,206	\$ 53,804
Bond Reserve Fund	115,000	115,000
Total	<u>\$ 170,206</u>	<u>\$ 168,804</u>

Monthly deposits into the bond sinking fund are required to establish the amount necessary to pay the next installments of principal and interest. The bond reserve fund at December 31, 2010 and 2009 equaled the required balance; therefore monthly deposits into the fund are not currently required. These funds may be used to pay principal and interest payments when insufficient funds are available in the sinking fund.

**MUNICIPAL WATER UTILITY
OF THE CITY OF SPENCER, IOWA
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2010 AND 2009**

Note 8 - RATE MATTERS

Rates of the Utility are established by the Board of Trustees and, as a municipal system, are not subject to the regulation of the Utilities Division of the Department of Commerce of the State of Iowa.

Note 9 - NUMBER OF METER CONNECTIONS

The number of meter connections totaled 5,826 and 5,714 at December 31, 2010 and 2009, respectively.

Note 10 - LEASES

The Utility leases building space to the Electric Utility and Communications Utility. The revenues from such leases are classified as leased facilities. The leases are monthly leases based on building space utilized and totaled \$11,968 in 2010 and 2009. The receivable at December 31, 2010 and 2009 was \$11,968 each year.

The Utility lease bandwidth and building space from the Electric and Communications Utilities. The expense from such leases is classified as operating expense. The lease is a 20-year variable lease based on bandwidth and space utilized and totaled \$21,658 and \$23,418 in 2010 and 2009. The payable at December 31, 2010 and 2009 was \$21,658 and \$23,418, respectively.

Note 11 - RETIREMENT SYSTEM

IPERS

The Utility contributes to the Iowa Public Employees Retirement System (IPERS) which is a cost-sharing, multiple-employer defined benefit pension plan administered by the State of Iowa. IPERS provides retirement and death benefits which are established by state statute to plan member and beneficiaries. IPERS issues a publicly available financial report that includes financial statements and required supplementary information. The report may be obtained by writing to IPERS, PO Box 9117, Des Moines, Iowa, 50306-9117.

Plan members were required to contribute 4.30% through June 30, 2010 and 4.50% presently of their annual salary and the Utility was required to contribute 6.65% through June 30, 2010 and 6.95% presently of annual payroll. Contribution requirements are established by State statute. The Utility's contributions to IPERS for the years ended December 31, 2010, 2009 and 2008 were \$21,060, \$19,305 and \$17,880, respectively, equal to the required contributions for each year.

**MUNICIPAL WATER UTILITY
OF THE CITY OF SPENCER, IOWA
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2010 AND 2009**

Note 11 - RETIREMENT SYSTEM(Continued)

EMPLOYEES PENSION PLAN

All full-time employees of the Water Utility who have completed six months of continuous employment and are 18 years of age are eligible to participate in a 457b Pension Plan administered by Security National Bank. The Utility contributes 8% of the employees' compensation for all employees contributing at least 2% of their salary.

The Water Utility's contribution to the Money Accumulation Pension Plan for 2010 and 2009 totaled \$20,599 and \$21,321, respectively.

Note 12 - OTHER POST EMPLOYMENT BENEFITS

During fiscal 2008, the Utility adopted the provisions of GASB 45 "Accounting and Financial Reporting by Employers for Post-Employment Benefits Other Than Pensions". The major change under GASB 45 is to attribute the cost of post-employment benefits to the time during which the employee is working for the employer. Accordingly, a prospective liability is recorded at June 30, 2010 for a Post-Employment Benefit Obligation as determined by an actuarial calculation.

Plan Description. The Utility operates a single-employer retiree benefit plan which provides medical/prescription drug benefits for retirees and their family.

The medical/prescription drug coverage is provided through a fully-insured plan. Retirees under age 65 pay the same premium for the medical/prescription drug benefit as active employees, which results in a implicit subsidy and an OPEB liability.

Funding Policy. The Utility currently finances the retiree benefit plan on a pay-as-you-go basis.

Annual OPEB Cost and NET OPEB Obligation. The Utility's annual other post-employment benefit (OPEB) cost is calculated based on the annual required contribution of the employer (ARC), an amount actuarially determined in accordance with the parameters of GASB 45. The ARC represents a level of funding that, if paid on an ongoing basis, is projected to cover normal cost each year and amortize any unfunded actuarial liabilities over a period not to exceed thirty years.

The following table shows the components of the Utility's annual OPEB for the year, the amount actually contributed to the plan, and changes in the Utility's net OPEB obligation to the plan:

	<u>2010</u>	<u>2009</u>
Annual required contribution	\$ 2,431	\$ 2,164
Interest on net OPEB obligation	166	81
Adjustment to annual required contribution	<u>(164)</u>	<u>(117)</u>
Annual OPEB cost (Expense)	2,433	2,128
Contributions made	<u>(13)</u>	<u>(11)</u>
Increase in net OPEB obligation	2,420	2,117
Net OPEB obligation - beginning of year	<u>4,138</u>	<u>2,021</u>
Net OPEB obligation - end of year	<u><u>\$ 6,558</u></u>	<u><u>\$ 4,138</u></u>

**MUNICIPAL WATER UTILITY
OF THE CITY OF SPENCER, IOWA
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2010 AND 2009**

Note 12 – OTHER POST EMPLOYMENT BENEFITS (Continued)

The Utility's annual OPEB cost, the percentage of annual OPEB cost contributed to the plan, and the net OPEB obligation were as follows:

Fiscal Year Ended	Annual OPEB Cost	Percentage of Annual OPEB Cost Contributed	Net OPEB Obligation
2010	\$ 2,433	0.5%	\$ 6,558
2009	\$ 2,128	0.5%	\$ 4,138

Funded Status and Funding Progress. The funded status of the plan as of December 31, 2010 was as follows:

	2010	2009
Actuarial accrued liability (AAL)	\$16,680	\$13,726
Actuarial value of plan assets	-	-
Unfunded actuarial accrued liability (UAAL)	\$16,680	\$13,726
Covered payroll (active members)	\$382,033	\$370,906
UAAL as a percentage of covered payroll	4.4%	3.7%

Actuarial Methods and Assumptions. Actuarial valuations of an ongoing plan involve estimates of the value of reported amounts and assumptions about the probability of occurrence of events far into the future. Examples include assumptions about future employment, mortality, and the healthcare cost trend. Amounts determined regarding the funded status of the plan and the annual required contributions of the employer are subject to continual revision as actual results are compared with past expectations and new estimates are made about the future. The schedule of funding progress, presented as required supplementary information following the notes to the financial statements, presents multiyear trend information about whether the actuarial value of plan assets is increasing or decreasing over time relative to the actuarial accrued liabilities for benefits.

Projections of benefits for financial reporting purposes are based on the substantive plan and include the types of benefits provided at the time of each valuation and the historical pattern of sharing of benefit costs between the employer and plan members to that point and do not explicitly reflect the potential effect of legal or contractual funding limitation. The actuarial methods and assumptions used include techniques that are designed to reduce the effect of short-term volatility in actuarial accrued liabilities and the actuarial value of assets, consistent with the long-term perspective of the calculations.

**MUNICIPAL WATER UTILITY
OF THE CITY OF SPENCER, IOWA
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2010 AND 2009**

Note 12 – OTHER POST EMPLOYMENT BENEFITS (Continued)

In the December 31, 2010 actuarial valuation, the projected unit credit actuarial cost method was used. The actuarial assumptions included a 4% interest discount rate. The projected annual medical trend rate is 9%. The ultimate medical trend rate is 4.5%. The medical trend rate is reduced 0.5% each year until reaching the 4.5% ultimate trend rate.

Mortality rates are from the RP-2000 Combined Mortality Table projected to 2010 using Scale AA. The salary increase rate was assumed to be 3% per year. The UAAL is being amortized as a level dollar amount on an open basis over 30 years.

Note 13 - RISK MANAGEMENT

The Water Utility is exposed to various risks of loss related to torts; theft, damage to and destruction of assets; errors and omissions; injuries to employees; and natural disasters. These risks are covered by the purchase of commercial insurance. The Utility assumes liability for any deductible and claims in excess of coverage limitations. Settled claims from these risks have not exceeded commercial insurance coverage in any of the past three fiscal years.

Note 14 - RELATED PARTIES

The Electric Utility, Water Utility, and Communications Utility of the City of Spencer, Iowa exchange services in the normal course of business.

Two members of the Board of Trustees hold non-controlling interests in a financial institution where the Utility maintains cash balances.

Additional related party items are included in Note 10.

Note 15 – COMMITMENTS

Spencer Municipal Utilities entered into an agreement with Pittsburg Tank & Tower Co., Inc. in June 2010. The contract is in the amount of \$266,485 for improvements to the 1.5 million gallon water tank. The improvements include removal and replacement of the dome top and repainting of entire structure. Project completion should occur no later than July 2011.

**MUNICIPAL WATER UTILITY
OF THE CITY OF SPENCER, IOWA
BUDGETARY COMPARISON SCHEDULE OF RECEIPTS, DISBURSEMENTS
AND CHANGES IN NET ASSETS - BUDGET AND ACTUAL (CASH BASIS)
REQUIRED SUPPLEMENTARY INFORMATION
FOR YEAR ENDED DECEMBER 31, 2010**

	Budgeted	Actual	Final to Actual Variance
Receipts:			
Municipal Electric Utility		\$ 12,585,348	
Municipal Water Utility		1,410,463	
Municipal Communications Utility		7,612,073	
Total Receipts	\$ 24,186,800	21,607,884	\$ (2,578,916)
Expenditures:			
Municipal Electric Utility		13,000,336	
Municipal Water Utility		1,676,865	
Municipal Communications Utility		5,976,879	
Total Expenditures	23,228,800	20,654,080	2,574,720
Excess (Deficiency) of Revenues Over Expenditures	958,000	953,804	(4,196)
Other Financing Sources (Uses); Transfers Out	(2,600,000)	-	2,600,000
Net Change in Net Assets	(1,642,000)	953,804	2,595,804
Net Assets at Beginning of Year	17,684,388	17,684,388	-
Net Assets at End of Year	\$ 16,042,388	\$ 18,638,192	\$ 2,595,804

**MUNICIPAL WATER UTILITY
OF THE CITY OF SPENCER, IOWA
BUDGET TO GAAP RECONCILIATION
REQUIRED SUPPLEMENTARY INFORMATION
FOR YEAR ENDED DECEMBER 31, 2010**

	Cash Basis	Accrual Adjustments	Accrual Basis
Receipts:			
Municipal Electric Utility	\$ 12,585,348	\$ 207,810	\$ 12,793,158
Municipal Water Utility	1,410,463	154,321	1,564,784
Municipal Communications Utility	7,612,073	(1,890,260)	5,721,813
Total Receipts	<u>21,607,884</u>	<u>(1,528,129)</u>	<u>20,079,755</u>
Expenditures:			
Municipal Electric Utility	13,000,336	1,268,271	14,268,607
Municipal Water Utility	1,676,865	(118,211)	1,558,654
Municipal Communications Utility	5,976,879	891,731	6,868,610
Total Expenditures	<u>20,654,080</u>	<u>2,041,791</u>	<u>22,695,871</u>
 Net Change in Net Assets	 953,804	 (3,569,920)	 (2,616,116)
 Net Assets at Beginning of Year	 <u>17,684,388</u>	 <u>45,995,135</u>	 <u>63,679,523</u>
 Net Assets at End of Year	 <u><u>\$ 18,638,192</u></u>	 <u><u>\$ 42,425,215</u></u>	 <u><u>\$ 61,063,407</u></u>

**MUNICIPAL WATER UTILITY
OF THE CITY OF SPENCER, IOWA
NOTES TO REQUIRED SUPPLEMENTARY INFORMATION –
BUDGETARY REPORTING
YEAR ENDED DECEMBER 31, 2010**

The budgetary comparison is presented as Required Supplementary Information in accordance with Government Accounting Standards Board Statement No. 41 for governments with significant budgetary perspective differences resulting from not being able to present budgetary comparisons for each individual utility.

In accordance with the Code of Iowa, Spencer Municipal Utilities annually adopts a combined budget on the cash basis for the Municipal Electric Utility, Municipal Water Utility, and Municipal Communications Utility of the City of Spencer, Iowa following required public notice and hearing. The annual budget may be amended during the year utilizing similar statutorily prescribed procedures. Encumbrances are not recognized and appropriations lapse at year-end.

**MUNICIPAL WATER UTILITY
OF THE CITY OF SPENCER, IOWA
FUNDING PROGRESS FOR THE RETIREE HEALTH PLAN
FOR YEAR ENDED DECEMBER 31, 2010**

Year Ended December 31,	Actuarial Valuation Date	Actuarial Value of Assets (a)	Actuarial Accrued Liability (AAL) (b)	Unfunded AAL (UAAL) (b-a)	Funded Ratio (a/b)	Covered Payroll (c)	UAAL as a Percentage of Covered Payroll ((b-a)/c)
2008	12/31/2008	\$ -	\$ 11,713	\$ 11,713	0%	\$ 360,103	3.3%
2009	12/31/2009	\$ -	\$ 13,726	\$ 13,726	0%	\$ 370,906	3.7%
2010	12/31/2010	\$ -	\$ 16,680	\$ 16,680	0%	\$ 382,033	4.4%

See Note 12 to the accompanying Notes to Financial Statements for the plan description, funding policy, annual OPEB Cost and Net OPEB Obligation, and the funded status and funding progress.

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**INDEPENDENT AUDITORS' REPORT ON INTERNAL CONTROL OVER
FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS
BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN
ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS**

To the Board of Trustees
Spencer Municipal Utilities – Municipal Water Utility
Spencer, Iowa 51301

We have audited the accompanying financial statements of Municipal Water Utility of the City of Spencer, Iowa (Spencer Municipal Utility) as of and for the year ended December 31, 2010, which collectively comprise the Utility's basic financial statements listed in the table of contents, and have issued our report thereon dated April 5, 2011. We conducted our audit in accordance with U.S. generally accepted auditing standards and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered Spencer Municipal Utility's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing our opinion on the effectiveness of Spencer Municipal Utility's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of Spencer Municipal Utility's internal control over financial reporting.

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and would not necessarily identify all deficiencies in internal control over financial reporting that might be significant deficiencies or material weaknesses. However, as discussed below, we identified a certain deficiency in internal control over financial reporting that we consider to be a material weakness.

A deficiency in internal control exists when the design or operation of the control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect and correct misstatements on a timely basis. A material weakness is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility a material misstatement of the Utility's financial statements will not be prevented or detected and corrected on a timely basis. We consider the deficiency in internal control described in Part II of the accompanying Schedule of Findings as item II-A-10 to be a material weakness in internal control over financial reporting.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether Spencer Municipal Utility's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grants, non-compliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of non-compliance or other matters that are required to be reported under *Government Auditing Standards*.

Spencer Municipal Utility's responses to findings identified in our audit are described in the accompanying Schedule of Findings and Questioned Costs. While we have expressed our conclusions on the Utility's responses, we did not audit Spencer Municipal Utility's responses, and accordingly, we express no opinion on them.

This report, a public record by law, is intended solely for the information and use of the officials, employees and citizens of Spencer Municipal Utility and other parties to whom Spencer Municipal Utility may report, including federal awarding agencies and pass-through entities. This report is not intended to be and should not be used by anyone other than these specified parties.

We would like to acknowledge the many courtesies and assistance extended to us by personnel of Spencer Municipal Utility during the course of our audit. Should you have any questions concerning any of the above matters, we shall be pleased to discuss them with you at your convenience.

Williams & Company, P.C.
Certified Public Accountants

Spencer, Iowa
April 5, 2011

**SPENCER MUNICIPAL UTILITIES
MUNICIPAL WATER UTILITY
SCHEDULE OF FINDINGS
FOR THE YEAR ENDED DECEMBER 31, 2010**

Part I: Summary of the Independent Auditors' Results:

- (a) An unqualified opinion was issued on the financial statements.
- (b) A significant deficiency in internal control over financial reporting was disclosed by the audit of the financial statements and is considered to be a material weakness.
- (c) The audit did not disclose any noncompliance which is material to the financial statements.

Part II: Findings Related to the General Purpose Financial Statements

SIGNIFICANT DEFICIENCY:

II-A-10 Financial Reporting – During the audit, we identified immaterial adjustments which could result in material misstatements of cash, accounts receivable, fixed assets and accounts payable not initially identified by Spencer Municipal Utility's internal control. These amounts were either not recorded or not properly recorded in Spencer Municipal Utility's financial statements. Adjustments were subsequently made by Spencer Municipal Utility, if applicable, to properly include or reclassify these amounts in the financial statements.

Recommendation – Spencer Municipal Utility should implement procedures to ensure all accounts are properly identified, classified, and included in Spencer Municipal Utility's financial statements.

Response – We will revise our current procedures to ensure the proper amounts are recorded in the financial statements in the future.

Conclusion - Response accepted.

INSTANCES OF NONCOMPLIANCE:

No matters were reported.

**SPENCER MUNICIPAL UTILITIES
MUNICIPAL WATER UTILITY
SCHEDULE OF FINDINGS
YEAR ENDED DECEMBER 31, 2010**

Part III: Other Findings Related to Required Statutory Reporting

III-A-10 Certified Budget – Disbursements during the year ended December 31, 2010 did not exceed the amounts budgeted in the business type activities function.

III-B-10 Questionable Expenditures – We noted no expenditures that we believe may not meet the requirements of public purpose as defined in an Attorney General's opinion dated April 25, 1979.

III-C-10 Travel Expenses – No expenditures of Utility's money for travel expenses of spouses of Utility's officials or employees were noted.

III-D-10 Business Transactions – Business transactions between Utility and Utility officials and employees are detailed as follows:

<u>Name, Title and Business Connection</u>	<u>Transaction Description</u>	<u>Amount</u>
Tom Howe, Board Member		
Part owner of H & N Chevrolet	Maintenance & Repairs	46

In accordance with Chapter 362.5(10) of the Code of Iowa, the transactions with the Board Member do not appear to represent conflicts of interest since total transactions with each were less than \$1,500 during the year.

III-E-10 Bond Coverage – Surety bond coverage of Spencer Municipal Utilities' officials and employees is in accordance with statutory provisions. The amount of coverage should be reviewed annually to insure that the coverage is adequate for current operations.

III-F-10 Board Minutes – No transactions were found that we believe should have been approved in the Board minutes but were not.

III-G-10 Revenue Bonds – As of December 31, 2010 the Utility is in compliance with all bond covenant requirements.

III-H-10 Deposits and Investments – No instances of non-compliance with the deposit and investment provisions of Chapter 12(B) and 12(c) of the Code of Iowa and the Utility's investment policy were noted.

SPENCER MUNICIPAL UTILITIES
MUNICIPAL COMMUNICATIONS UTILITY
OF THE CITY OF SPENCER, IOWA

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INDEPENDENT AUDITORS' REPORT

Board of Trustees
Spencer Municipal Utilities – Municipal Communications Utility
Spencer, IA 51301

We have audited the accompanying financial statements of the business-type activity of Municipal Communications Utility of the City of Spencer, Iowa (the Utility), as of and for the year ended December 31, 2010, which collectively comprise the Utility's basic financial statements as listed in the table of contents. These financial statements are the responsibility of management. Our responsibility is to express an opinion on these financial statements based on our audit. The prior year comparative information has been derived from the Utility's 2009 financial statements and, in our report dated May 6, 2010, we expressed an unqualified opinion on the respective financial statements of the business-type activity.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatements. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the business-type activity of the Utility as of December 31, 2010 and the respective changes in financial position and cash flows for the year then ended, in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated April 5, 2011, on our consideration of the Utility's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards*, and should be considered in conjunction with this report in considering the results of our audit.

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis, budgetary comparison and funding progress for the retiree health plan information on pages 64 through 66 and pages 80 through 83 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Williams & Company, P.C.
Certified Public Accountants

Spencer, Iowa
April 5, 2011

MANAGEMENT'S DISCUSSION AND ANALYSIS

The purpose of management's discussion and analysis (MD&A) is to provide the reader with an introduction to the financial statements. Our discussion and analysis of the Municipal Communications Utility (Utility) of the City of Spencer, Iowa's financial performance provides an overview of the Utility's financial activities for the years ended December 31, 2010 and 2009.

The following information should be read in conjunction with the financial statements and the accompanying notes to the financial statements that follow this section.

2010 Financial Highlights

Total assets decreased by approximately \$953,000 which was attributable to depreciation exceeding assets placed in service.

Total net assets decreased by \$1,146,797 as the result of the utility operations.

Overview of the Financial Statements

The balance sheets include the Utility's assets and liabilities and provide information about the nature and amounts of investments in resources (assets) and the obligations to creditors (liabilities).

The statement of revenues, expenses and changes in net assets report all revenues and expenses incurred during the fiscal year.

The Statement of Cash Flows present cash receipts, cash disbursements, and net changes in cash resulting from operations, capital and related financing activities and investing activities.

The notes to the financial statements provide the required disclosures and other information that is necessary to give the reader a complete understanding of the data provided in the statements. The notes present information about the Utility's accounting policies, material risks, obligations, commitments, contingencies and subsequent events.

Condensed Financial Information

The following condensed financial information serves as the key financial data and indicators for management, monitoring, and planning.

Condensed Statements of Net Assets

	<u>2010</u>	<u>2009</u>
Current assets	\$7,258,652	\$7,523,299
Capital assets, net of depreciation	4,563,215	5,250,702
Noncurrent assets	<u>771,315</u>	<u>772,470</u>
Total assets	<u>\$12,593,182</u>	<u>\$13,546,471</u>
Current liabilities	\$1,323,303	\$1,127,395
Long-term debt	<u>3,042,000</u>	<u>3,044,400</u>
Total liabilities	<u>4,365,303</u>	<u>4,171,795</u>
Invested in capital assets, net of related debt	1,563,215	2,250,702
Unrestricted	<u>6,664,664</u>	<u>7,123,974</u>
Total net assets	<u>8,227,879</u>	<u>9,374,676</u>
Total liabilities and net assets	<u>\$12,593,182</u>	<u>\$13,546,471</u>

Condensed Statement of Revenues, Expenses and Changes in Net Assets

Cable television revenue	\$1,763,505	\$1,426,881
Telephone revenue	2,291,717	3,930,105
Data revenue	1,352,263	1,256,262
Miscellaneous revenue	<u>12,797</u>	<u>12,049</u>
Total operating revenue	<u>5,420,282</u>	<u>6,625,297</u>
System operation & maintenance	3,774,548	3,851,669
Depreciation & amortization	1,150,833	1,131,215
Customer service & administration	<u>1,137,567</u>	<u>934,532</u>
Total operating expenses	<u>6,062,948</u>	<u>5,917,545</u>
Operating income (loss)	(642,666)	707,572
Interest income	21,575	29,412
Interest expense	(137,800)	(137,191)
Other income (expense)	<u>(387,906)</u>	<u>(30,861)</u>
Total non-operating revenues	<u>(504,131)</u>	<u>(138,640)</u>
Change in net assets	(1,146,797)	569,112
Net assets, beginning of year	<u>9,374,676</u>	<u>8,805,564</u>
Net assets, end of year	<u>\$8,227,879</u>	<u>\$9,374,676</u>

Financial Analysis

The Utility's total assets decreased by approximately \$953,000.

The Utility's gross revenues decreased by approximately \$1,205,000 or 18%. Telephone sales revenue decreased by \$1,638,000 primarily due to an increase in the access allowance expense associated with the conference partner payable. CATV sales increased by \$337,000 due to rate increases implemented in October 2009 and 2010 in combination with steady customer growth.

Total operating expenses increased by approximately \$145,000 due to an increase in legal fees and addition of Human Resources Coordinator.

Total operating loss generated in 2010 was approximately \$(643,000) compared to operating income of approximately \$708,000 in 2009.

The Utility had a net loss of (\$1,146,797) for the year ended December 31, 2010 compared to a net income of \$569,112 for the year ended December 31, 2009. The change was attributable to the Qwest access write off.

Capital Assets and Debt Administration

Net capital assets decreased by approximately \$687,000 and \$639,000 for years ending December 31, 2010 and 2009, respectively. This was due to depreciation exceeding assets placed in service for both years ending December 31, 2010 and 2009.

Economic Factors

The Utility continues to see stable growth in subscriber base. The Utility will be faced with increased costs of operating due to cable programming contracts. Although the Verizon lawsuit was settled, uncertainty remains as to the outcome of legal litigation concerning collectable access revenues with Sprint, AT&T and Qwest. Management remains conservative in estimating access collectable balance.

Contacting the Utility's Financial Management

This financial report is designed to present our citizens, customers, and creditors with a general overview of the Utility's finances and operating activities. If you have any questions or require additional information please contact the Finance Supervisor, 712 Grand Ave, PO Box 222, Spencer, Iowa 51301.

**MUNICIPAL COMMUNICATIONS UTILITY
OF THE CITY OF SPENCER, IOWA
STATEMENTS OF NET ASSETS
DECEMBER 31, 2010 AND 2009**

	2010	2009
ASSETS		
Current Assets:		
Cash and Cash Equivalents	\$ 5,262,288	\$ 3,627,094
Consumer Deposits	63,028	61,924
Accounts Receivable	1,597,761	3,345,348
Unbilled Usage	201,220	350,746
Materials And Supplies Inventory	85,685	74,857
Prepayments and Other	48,670	63,330
Total Current Assets	7,258,652	7,523,299
Capital Assets:		
Land	10,342	10,342
Property and Equipment	12,612,204	12,157,473
Accumulated Depreciation	(8,059,331)	(6,917,113)
Total Capital Assets	4,563,215	5,250,702
Noncurrent Assets:		
Unamortized Bond Issue Costs	5,996	10,792
Long-term Receivables	765,319	761,678
Total Noncurrent Assets	771,315	772,470
Total Assets	12,593,182	13,546,471
LIABILITIES AND NET ASSETS		
Current Liabilities:		
Accounts Payable	1,152,900	998,713
Payroll and Sales Tax Payable	20,374	8,063
Accrued Payroll and Compensated Absences	84,601	56,295
Deferred Revenue	2,400	2,400
Consumer Deposits	63,028	61,924
Total Current Liabilities	1,323,303	1,127,395
Noncurrent Liabilities		
Deferred Revenue	42,000	44,400
Note Payable	3,000,000	3,000,000
Total Noncurrent Liabilities	3,042,000	3,044,400
Total Liabilities	4,365,303	4,171,795
Net Assets		
Invested in Capital Assets, Net of Related Debt	1,563,215	2,250,702
Unrestricted	6,664,664	7,123,974
Total Net Assets	\$ 8,227,879	\$ 9,374,676

See Accompanying Notes to Financial Statements

**MUNICIPAL COMMUNICATIONS UTILITY
OF THE CITY OF SPENCER, IOWA
STATEMENTS OF REVENUES, EXPENSES AND
CHANGES IN FUND NET ASSETS
FOR THE YEARS ENDED DECEMBER 31, 2010 AND 2009**

	2010	2009
Operating Revenues:		
Cable System Revenue	\$ 1,763,505	\$ 1,426,881
Telephone System Revenue	2,291,717	3,930,105
Data Services Revenue	1,352,263	1,256,262
Miscellaneous Income	12,797	12,049
Total Operating Revenues	5,420,282	6,625,297
Operating Expenses:		
Plant Specific and Programming	3,774,548	3,851,798
Depreciation and Amortization	1,150,833	1,131,215
Customer Services and Marketing	480,457	475,981
General and Administrative	657,110	458,551
Total Operating Expenses	6,062,948	5,917,545
Operating Income (Loss)	(642,666)	707,752
Non-Operating Income (Expense):		
Leased Facilities	188,116	177,817
Net Income from Joint Ventures	85,931	46,766
Economic Development Payment	(27,594)	(1,647)
Interest Income	21,575	29,412
Interest Expense	(137,800)	(137,191)
Inventory Sales	5,101	3,254
Gain on Plant Retirements	808	650
Payment in Lieu of Property Taxes	(640,268)	(257,701)
Total Non-Operating Income (Expense)	(504,131)	(138,640)
Changes in Net Assets	(1,146,797)	569,112
Net Assets at Beginning of Year	9,374,676	8,805,564
Net Assets at End of Year	\$ 8,227,879	\$ 9,374,676

See Accompanying Notes to Financial Statements

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**MUNICIPAL COMMUNICATIONS UTILITY
OF THE CITY OF SPENCER, IOWA
STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED DECEMBER 31, 2010 AND 2009**

	<u>2010</u>	<u>2009</u>
Cash Flows From Operating Activities:		
Cash Received From Customers	\$ 7,313,891	\$ 4,983,857
Cash Payments to Suppliers for Goods and Services	(3,280,544)	(3,372,050)
Cash Payments to Employees for Services	(1,431,831)	(1,353,652)
Cash Payments for Economic Development and In Lieu of Property Taxes	(667,862)	(259,348)
Payments Received From Leasing of Facilities	188,116	177,817
Net Cash Provided By Operating Activities	<u>2,121,770</u>	<u>176,624</u>
Cash Flows From Capital and Related Financing Activities:		
Acquisition & Construction of Property and Equipment	(458,842)	(488,354)
Proceeds from Sale of Capital Assets	1,100	1,200
Payments Received From Sale of Inventory	5,101	3,254
Interest Paid	(137,800)	(137,191)
Net Cash (Used) By Capital and Related Financing Activities	<u>(590,441)</u>	<u>(621,091)</u>
Cash Flows From Investing Activities:		
Other Investments	82,290	6,784
Interest Received From Investments	21,575	29,412
Net Cash Provided By Investing Activities	<u>103,865</u>	<u>36,196</u>
Net Increase (Decrease) in Cash	1,635,194	(408,271)
Cash and Cash Equivalents at Beginning of Year	<u>3,627,094</u>	<u>4,035,365</u>
Cash and Cash Equivalents at End of Year	<u><u>\$ 5,262,288</u></u>	<u><u>\$ 3,627,094</u></u>

See Accompanying Notes to Financial Statements

**MUNICIPAL COMMUNICATIONS UTILITY
OF THE CITY OF SPENCER, IOWA
STATEMENTS OF CASH FLOWS (CONTINUED)
FOR THE YEARS ENDED DECEMBER 31, 2010 AND 2009**

**Reconciliation of Operating Income (Loss) to Net
Cash Provided by Operating Activities**

Operating Income (Loss)	\$	(642,666)	\$	707,752
Adjustments to Reconcile Operating Income (Loss) to Net Cash Provided By Operating Activities				
Depreciation and Amortization		1,150,833		1,131,215
Leased Facilities Income		188,116		177,817
Contributions Paid for Economic Development		(27,594)		(1,647)
Payment in Lieu of Property Taxes		(640,268)		(257,701)
(Increase) Decrease in Operating Assets:				
Consumer Deposits		(1,104)		1,405
Accounts Receivable		1,747,587		(1,921,750)
Unbilled Usage		149,526		232,105
Materials and Supplies Inventory		(10,828)		(18,203)
Prepayments		14,660		(25,022)
Increase (Decrease) in Operating Liabilities:				
Accounts Payable		154,187		124,272
Accrued Payroll and Compensated Absences		40,617		(19,014)
Consumer Deposits		1,104		(1,405)
Deferred Revenue		(2,400)		46,800
Total Adjustments		<u>2,764,436</u>		<u>(531,128)</u>
Net Cash Provided By Operating Activities	\$	2,121,770	\$	176,624

See Accompanying Notes to Financial Statements

**MUNICIPAL COMMUNICATIONS UTILITY
OF THE CITY OF SPENCER, IOWA
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2010 AND 2009**

Note 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

A. Organization and Basis of Accounting

The Municipal Communications Utility of the City of Spencer, Iowa (Communications Utility or Utility) operates as an independent unit of the City of Spencer and is managed, along with the Municipal Electric Utility and the Municipal Water Utility of the City of Spencer, Iowa, by a five member Board of Trustees. The Utility was formed to engage in the development and operation of a broadband communications system and the marketing of related services such as cable television, telephone, high-speed data communications and other communication products. The Utility's rates are set by its governing board.

For financial reporting purposes, the Utility has included all funds. The Utility has also considered all potential component units for which it is financially accountable, and other organizations for which the nature and significance of their relationship with the Utility are such that exclusion would cause the Utility's financial statements to be misleading or incomplete. The Governmental Accounting Standards Board has set forth criteria to be considered in determining financial accountability. These criteria include appointing a voting majority of an organization's governing body, and (1) the ability of the Utility to impose its will on that organization or (2) the potential for the organization to provide specific benefits to, or impose specific financial burdens on the Utility. It was determined that the Utility has no component units.

The Utility is not considered to be a component unit of the City of Spencer for financial statement purposes.

The Utility's financial statements are reported using the economic resources measurement focus and the accrual basis of accounting. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows.

In reporting the financial activity of its enterprise fund, the Utility applies all applicable GASB pronouncements as well as the following pronouncements issued on or before November 30, 1989, unless these pronouncements conflict with or contradict GASB pronouncements: Financial Accounting Standards Board Statements and Interpretations, Accounting Principles Board Opinions, and Accounting Research Bulletins of the Committee on Accounting Procedure.

The Utility distinguishes operating revenues and expenses from non-operating items. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with the Utility's principal ongoing operations. The principal operating revenues of the Utility are charges to customers for sales and services. Operating expenses include the cost of sales and services, administrative expenses, and depreciation on capital assets. All revenues and expenses not meeting this definition are reported as non-operating revenues and expenses.

**MUNICIPAL COMMUNICATIONS UTILITY
OF THE CITY OF SPENCER, IOWA
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2010 AND 2009**

Note 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

B. Capital Assets and Depreciation

Capital assets are stated at original cost when first devoted to public service. Currently, such costs include labor-related expenditures, such as payroll taxes, pensions, and other fringe benefits and administrative costs for labor related to the construction of new communications facilities. In addition, net interest costs on construction debt are capitalized. Replacements and betterments of capital assets are charged to capital assets. Routine maintenance and repairs are charged to expense as incurred. Depreciation is calculated on the straight-line basis. Current depreciation expense is approximately 10.15% of the original cost of depreciable communication plant in service.

The estimated useful lives used to depreciate assets by class are as follows:

Infrastructure	10-15 years
Buildings and improvements	20 years
Equipment	5-7 years

C. Accounts Receivable

Accounts receivable are stated at the amount the Utility expects to collect from outstanding balances. The Utility provides for probable uncollectible amounts through a charge to earnings and a credit to a valuation allowed based on its assessment of the current status of individual accounts. Balances that are still outstanding after the Utility has used reasonable collection efforts are written off through a charge to the valuation allowance and a credit to accounts receivable. Changes in the valuation allowance have not been material to the financial statements.

D. Inventories

Inventories are valued at the lower of cost or market. The average cost method is used for determining the cost of materials and supplies inventory. Inventories are recorded as an expenditure or, if applicable, capitalized when consumed.

E. Unamortized Deferred Costs

Cable television system costs allocated during construction of the system are being amortized using the straight-line method over the expected life of the cable television plant.

F. Net Assets

Net assets represent the difference between assets and liabilities in the financial statements. Net assets invested in capital assets, net of related debt, consists of capital assets, net of accumulated depreciation, reduced by the outstanding balance of any long-term debt used for acquisition, construction or improvement of those assets and increased by unspent debt when there are limitations imposed on their use through external restrictions imposed by creditors, grantors or laws or regulations of other governments.

**MUNICIPAL COMMUNICATIONS UTILITY
OF THE CITY OF SPENCER, IOWA
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2010 AND 2009**

Note 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

The Utility's policy is to first apply restricted resources when an expense is incurred for purposes for which both restricted and unrestricted net assets are available.

G. Income Taxes

The Communications Utility is exempt from federal and state income taxes because it is a governmental entity organized under the provisions of Chapter 388 of the Code of Iowa.

H. Revenues and Unbilled Usage

Revenues are based on billing rates, which are applied to customers' consumption of communications services. The Utility records estimated unbilled revenue at the end of accounting periods. Revenues earned, but not yet billed at December 31, 2010 and 2009, totaled \$201,130 and \$350,746, respectively.

I. Estimates

The preparation of the financial statements in conformity with U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results may differ from those estimates.

Note 2 - CASH AND CASH EQUIVALENTS

The Utility's deposits in banks at December 31, 2010 and 2009 were entirely covered by federal depository insurance or by the State Sinking Fund in accordance with Chapter 12C of the Code of Iowa. This chapter provides for additional assessments against the depositories to insure there will be no loss of public funds.

The Utility is authorized by statute and Board of Trustees' approval to invest public funds in obligations of the United States government, its agencies, and instrumentalities; certificates of deposit and other evidences of deposit at federally insured Iowa depository institutions; and the Iowa Public Agency Investment Trust.

Interest Rate Risk – The Utility's investment policy limits the investment of operating funds (funds expected to be expended in the current budget year or within 15 months of receipt) in instruments that mature within 397 days. Funds not identified as operating funds may be invested in investments with maturities longer than 397 days, but the maturities shall be consistent with the needs and use of the Utility.

Credit Risk – The Utility's investments consisted of Certificate of Deposits are protected per Chapter 12C of the Iowa Code, and credit risk and concentration risks do not apply.

The Utility considers all highly liquid investments with an original maturity of three months or less to be cash equivalents for purposes of the statement of cash flows.

**MUNICIPAL COMMUNICATIONS UTILITY
OF THE CITY OF SPENCER, IOWA
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2010 AND 2009**

Note 3 - CAPITAL ASSETS

Capital assets activity for the year ended December 31, 2010 was as follows:

	Beginning Balance	Additions and Transfers In	Deletions and Transfers Out	Ending Balance
Capital assets not being depreciated:				
Land	\$ 10,342	\$ -	\$ -	\$ 10,342
Total capital assets not being depreciated	10,342	-	-	10,342
Capital assets being depreciated:				
Infrastructure	10,168,875	218,291	-	10,387,166
Buildings and improvements	943,600	1,177	-	944,777
Equipment	1,044,998	239,375	(4,112)	1,280,261
Total capital assets being depreciated	12,157,473	458,843	(4,112)	12,612,204
Less accumulated depreciation	6,917,113	1,146,037	(3,819)	8,059,331
Total capital assets being depreciated - net	5,240,360	(687,193)	(293)	4,552,873
Capital assets - net	\$5,250,702	\$ (687,193)	\$ (293)	\$4,563,215

Capital assets activity for the year ended December 31, 2009 was as follows:

	Beginning Balance	Additions and Transfers In	Deletions and Transfers Out	Ending Balance
Capital assets not being depreciated:				
Land	\$ 10,342	\$ -	\$ -	\$ 10,342
Total capital assets not being depreciated	10,342	-	-	10,342
Capital assets being depreciated:				
Infrastructure	9,813,558	358,459	(3,142)	10,168,875
Buildings and improvements	882,848	85,577	(24,825)	943,600
Equipment	975,854	69,144	-	1,044,998
Total capital assets being depreciated	11,672,260	513,180	(27,967)	12,157,473
Less accumulated depreciation	5,793,287	1,126,418	(2,592)	6,917,113
Total capital assets being depreciated - net	5,878,973	(613,238)	(25,375)	5,240,360
Capital assets - net	\$ 5,889,315	\$ (613,238)	\$ (25,375)	\$5,250,702

**MUNICIPAL COMMUNICATIONS UTILITY
OF THE CITY OF SPENCER, IOWA
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2010 AND 2009**

Note 4 - TRANSFERS IN LIEU OF PROPERTY TAX

By resolution of the Board of Trustees, voluntary transfers in lieu of property taxes are made to the City of Spencer, Iowa. Funds totaling \$640,268 and \$257,701 were transferred to the City during 2010 and 2009, respectively.

Note 5 - LONG-TERM RECEIVABLES

During December 2003, the Utility entered into an agreement with Northern Iowa Communications Partners, LLC (NICP), an Iowa limited liability company, pursuant to the provisions of Chapter 28E of the Code of Iowa. Under this agreement, the Utility, along with other members of NICP, agrees to pay for the use of a shared switch for routing certain telecommunications traffic at rates adopted by NICP. The Utility will share in profits generated or shortfalls incurred through the 28E agreement due to the method used to determine an annual usage fee paid by NICP to the Utility. An NICP member will be responsible for maintaining the financial records related to the 28E agreement. The amount earned but not received by the Utility in 2010 and 2009 was \$231,704 and \$248,525, respectively. These amount are recorded as a receivable.

During May 2006, the Utility entered into an agreement with Evertek, Inc., an Iowa Corporation, to create Clay County Communications, LLC as a separate legal entity. Clay County Communications shall function as if it were a limited liability company organized under Iowa Code Chapter 490A. The purpose of this agreement and Clay County Communications is to provide wired and/or wireless communications services in Clay County, Iowa. The Utility and Evertek, Inc. each initially contributed \$400,000. During 2007 the Utility and Evertek, Inc. each made an additional contribution \$150,000. The Utility accounts for the joint venture on the equity method, and has recorded the balance of \$533,615 and \$513,153 as a receivable in 2010 and 2009 respectively.

Note 6 – NOTE PAYABLE

Note payable activity for the year ended December 31, 2010 and 2009 was as follows:

	Beginning Balance	Additions	Reductions	Ending Balance	Amounts Due Within One Year
Note Payable - Municipal Electric Utility	\$ 3,000,000	\$ -	\$ -	\$ 3,000,000	\$ -

The Board of Trustees of the Municipal Electric Utility adopted a resolution on June 14, 1999, pursuant to Section 384.89 City Code of Iowa and Rule 2.5(5) of the rules promulgated by the City Finance Committee, allowing for the advance of funds not to exceed \$8,000,000 to the Municipal Communications Utility to be utilized for the construction and development of the communication system. These funds are to be repaid upon demand and bear a 4.5% per annum interest rate.

**MUNICIPAL COMMUNICATIONS UTILITY
OF THE CITY OF SPENCER, IOWA
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2010 AND 2009**

Note 7 – LEASES and LONG TERM DEFERRED REVENUE

Spencer Municipal Utilities entered into a 20 year fiber lease agreement with the Iowa Rural Health Telecommunications Program on July 1, 2009. The contract amount for the lease is \$48,000 and is due in full upon construction completion. Construction was completed and \$48,000 was collected in 2009. Spencer Municipal Utilities recognized \$1,200 and \$2,400 in revenue during 2009 and 2010, respectively. In 2010, there was \$2,400 as short term deferred revenue and the remaining \$42,000 as long term deferred revenue. Spencer Municipal Utilities is responsible for maintenance of the fiber.

The Utility leases building space from the Water Utility. The expense from the lease is classified as operating expense. The lease is a monthly lease based on building space utilized and totaled \$2,368 in 2010 and 2009. The payable at December 31, 2010 and 2009 was \$2,368.

The Utility leases bandwidth, property, and building space from the Electric Utility. The expense from the lease is classified as operating expense. The lease is a 20-year variable lease based on bandwidth and space utilized and totaled \$411,213 and \$410,668 in 2010 and 2009, respectively. The payable at December 31, 2010 and 2009 was \$411,213 and \$410,688, respectively.

Note 8 – RETIREMENT SYSTEM

IPERS

The Utility contributes to the Iowa Public Employees Retirement System (IPERS) which is a cost-sharing, multiple-employer defined benefit pension plan administered by the State of Iowa. IPERS provides retirement and death benefits which are established by state statute to plan members and beneficiaries. IPERS issues a publicly available financial report that includes financial statements and required supplementary information. The report may be obtained by writing to IPERS, PO Box 9117, Des Moines, Iowa, 50306-9117.

Plan members were required to contribute 4.30% through June 30, 2010 and 4.45% presently of their annual salary and the Utility was required to contribute 6.65% through June 30, 2010 and 6.95% presently of annual payroll. Contribution requirements are established by State statute. The Utility's contributions to IPERS for the years ended December 31, 2010, 2009 and 2008 were \$60,526, \$54,942 and \$48,928, respectively, equal to the required contributions for the year.

Employees Pension Plan

All full-time employees of the Communications Utility who have completed six months of continuous employment and are 18 years of age are eligible to participate in a 457b Pension Plan administered by Security National Bank. The Utility contributes 8% of the employees' compensation for all employees contributing at least 2% of their salary.

The Communications Utility's contribution to the Money Accumulation Pension Plan for 2010 and 2009 totaled \$65,080 and \$64,898, respectively.

**MUNICIPAL COMMUNICATIONS UTILITY
OF THE CITY OF SPENCER, IOWA
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2010 AND 2009**

Note 9 – OTHER POST EMPLOYMENT BENEFITS

During fiscal 2008, the Utility adopted the provisions of GASB 45 “Accounting and Financial Reporting by Employers for Post-Employment Benefits Other Than Pensions”. The major change under GASB 45 is to attribute the cost of post-employment benefits to the time during which the employee is working for the employer. Accordingly, a prospective liability is recorded at June 30, 2010 for a Post-Employment Benefit Obligation as determined by an actuarial calculation.

Plan Description. The Utility operates a single-employer retiree benefit plan which provides medical/prescription drug benefits for retirees and their family.

The medical/prescription drug coverage is provided through a fully-insured plan. Retirees under age 65 pay the same premium for the medical/prescription drug benefit as active employees, which results in a implicit subsidy and an OPEB liability.

Funding Policy. The Utility currently finances the retiree benefit plan on a pay-as-you-go basis.

Annual OPEB Cost and NET OPEB Obligation. The Utility’s annual other post-employment benefit (OPEB) cost is calculated based on the annual required contribution of the employer (ARC), an amount actuarially determined in accordance with the parameters of GASB 45. The ARC represents a level of funding that, if paid on an ongoing basis, is projected to cover normal cost each year and amortize any unfunded actuarial liabilities over a period not to exceed thirty years.

The following table shows the components of the Utility’s annual OPEB for the year, the amount actually contributed to the plan, and changes in the Utility’s net OPEB obligation to the plan:

	<u>2010</u>	<u>2009</u>
Annual required contribution	\$ 7,178	\$ 6,377
Interest on net OPEB obligation	482	238
Adjustment to annual required contribution	<u>(478)</u>	<u>(344)</u>
Annual OPEB cost (Expense)	7,182	6,271
Contributions made	<u>(197)</u>	<u>(178)</u>
Increase in net OPEB obligation	6,985	6,093
Net OPEB obligation - beginning of year	<u>12,039</u>	<u>5,946</u>
Net OPEB obligation - end of year	<u>\$ 19,024</u>	<u>\$ 12,039</u>

The Utility’s annual OPEB cost, the percentage of annual OPEB cost contributed to the plan, and the net OPEB obligation were as follows:

<u>Fiscal Year</u> <u>Ended</u>	<u>Annual</u> <u>OPEB Cost</u>	<u>Percentage of Annual OPEB</u> <u>Cost Contributed</u>	<u>Net OPEB</u> <u>Obligation</u>
2010	\$ 7,182	2.7%	\$ 19,024
2009	\$ 6,271	2.8%	\$ 12,039

**MUNICIPAL COMMUNICATIONS UTILITY
OF THE CITY OF SPENCER, IOWA
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2010 AND 2009**

Note 9 – OTHER POST EMPLOYMENT BENEFITS (Continued)

Funded Status and Funding Progress. The funded status of the plan as of December 31, 2010 was as follows:

	<u>2010</u>	<u>2009</u>
Actuarial accrued liability (AAL)	\$36,624	\$28,668
Actuarial value of plan assets	-	-
Unfunded actuarial accrued liability (UAAL)	<u>\$36,624</u>	<u>\$28,668</u>
 Covered payroll (active members)	 \$1,016,541	 \$986,933
UAAL as a percentage of covered payroll	3.6%	2.9%

Actuarial Methods and Assumptions. Actuarial valuations of an ongoing plan involve estimates of the value of reported amounts and assumptions about the probability of occurrence of events far into the future. Examples include assumptions about future employment, mortality, and the healthcare cost trend. Amounts determined regarding the funded status of the plan and the annual required contributions of the employer are subject to continual revision as actual results are compared with past expectations and new estimates are made about the future. The schedule of funding progress, presented as required supplementary information following the notes to the financial statements, presents multiyear trend information about whether the actuarial value of plan assets is increasing or decreasing over time relative to the actuarial accrued liabilities for benefits.

Projections of benefits for financial reporting purposes are based on the substantive plan and include the types of benefits provided at the time of each valuation and the historical pattern of sharing of benefit costs between the employer and plan members to that point and do not explicitly reflect the potential effect of legal or contractual funding limitation. The actuarial methods and assumptions used include techniques that are designed to reduce the effect of short-term volatility in actuarial accrued liabilities and the actuarial value of assets, consistent with the long-term perspective of the calculations.

In the December 31, 2010 actuarial valuation, the projected unit credit actuarial cost method was used. The actuarial assumptions included a 4% interest discount rate. The projected annual medical trend rate is 9%. The ultimate medical trend rate is 4.5%. The medical trend rate is reduced 0.5% each year until reaching the 4.5% ultimate trend rate.

Mortality rates are from the RP-2000 Combined Mortality Table projected to 2010 using Scale AA. The salary increase rate was assumed to be 3% per year. The UAAL is being amortized as a level dollar amount on an open basis over 30 years.

**MUNICIPAL COMMUNICATIONS UTILITY
OF THE CITY OF SPENCER, IOWA
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2010 AND 2009**

Note 10 - RISK MANAGEMENT

The Communications Utility is exposed to various risks of loss related to torts; theft, damage to and destruction of assets; errors and omissions; injuries to employees; and natural disasters. These risks are covered by the purchase of commercial insurance. The Utility assumes liability for any deductible and claims in excess of coverage limitations. Settled claims from these risks have not exceeded commercial insurance coverage in any of the past three fiscal years.

Note 11 - RELATED PARTIES

The Electric Utility, Water Utility, and Communications Utility of the City of Spencer, Iowa exchange services in the normal course of business. Two members of the Board of Trustees hold non-controlling interests in a financial institution where the Utility maintains cash balances.

Additional related party items are included in Notes 5, 6, and 7.

Note 12 – CONTINGENCIES

In the last four years, the Utility has provided Iowa based telephone numbers to callers who are then connected to a conference call. The Utility maintains these are terminated in Iowa and charges long-distance carriers a fee for terminating access services. The Utility then pays a portion of the revenue to other communication providers who supply a portion of the services. Until 2007 the long-distance carriers have paid these charges to the Utility and the Utility has paid the other communication providers. In 2007, Sprint, filed a lawsuit alleging that the calls are not terminated in Iowa, and that the Utility is not entitled to the terminating access charges that are billed to them. In 2010, the Utility filed a claim against AT&T for unpaid communications access. The Utility has filed counter-claims or claims against Sprint, Verizon, AT&T and Qwest so that the statute of limitations does not run out for filing counter claims. The Utility has also suspended its payments to the other providers pending the outcome of the litigation. Since 2008, the Utility has setup allowance accounts that reduce income and receivables to reflect management's estimate that it is reasonable to believe 15% of the gross revenues generated by terminating these long distance calls will be collected. During 2010, the calculated reserve was adjusted to reflect a settlement reached with one of the carries involved in the litigation, Verizon. This settlement exceeded the 15% calculated balance.

Note 13 - COMMITMENTS

Beginning in 2009, the Communications Utility pledged support to the Iowa Great Lakes Corridor of Opportunity at a level of \$25,000 per year for four years. This commitment is subject to annual review by the Utility Board.

Note 14 – SUBSEQUENT EVENT

On February 2, 2011 the Utility reached a settlement with a portion of the amount owed on the conference bridge account receivable with one of the communication providers. The settlement was in the amount of \$131,418.

**MUNICIPAL COMMUNICATIONS UTILITY
OF THE CITY OF SPENCER, IOWA
BUDGETARY COMPARISON SCHEDULE OF RECEIPTS, DISBURSEMENTS
AND CHANGES IN NET ASSETS - BUDGET AND ACTUAL (CASH BASIS)
REQUIRED SUPPLEMENTARY INFORMATION
FOR YEAR ENDED DECEMBER 31, 2010**

	Budgeted	Actual	Final to Actual Variance
Receipts:			
Municipal Electric Utility		\$ 12,585,348	
Municipal Water Utility		1,410,463	
Municipal Communications Utility		7,612,073	
Total Receipts	\$ 24,186,800	21,607,884	\$ (2,578,916)
Expenditures:			
Municipal Electric Utility		13,000,336	
Municipal Water Utility		1,676,865	
Municipal Communications Utility		5,976,879	
Total Expenditures	23,228,800	20,654,080	2,574,720
Excess (Deficiency) of Revenues Over Expenditures	958,000	953,804	(4,196)
Other Financing Sources (Uses); Transfers Out	(2,600,000)	-	2,600,000
Net Change in Net Assets	(1,642,000)	953,804	2,595,804
Net Assets at Beginning of Year	17,684,388	17,684,388	-
Net Assets at End of Year	\$ 16,042,388	\$ 18,638,192	\$ 2,595,804

**MUNICIPAL COMMUNICATIONS UTILITY
OF THE CITY OF SPENCER, IOWA
BUDGET TO GAAP RECONCILIATION
REQUIRED SUPPLEMENTARY INFORMATION
FOR YEAR ENDED DECEMBER 31, 2010**

	Cash Basis	Accrual Adjustments	Accrual Basis
Receipts:			
Municipal Electric Utility	\$ 12,585,348	\$ 207,810	\$ 12,793,158
Municipal Water Utility	1,410,463	154,321	1,564,784
Municipal Communications Utility	7,612,073	(1,890,260)	5,721,813
Total Receipts	<u>21,607,884</u>	<u>(1,528,129)</u>	<u>20,079,755</u>
Expenditures:			
Municipal Electric Utility	13,000,336	1,268,271	14,268,607
Municipal Water Utility	1,676,865	(118,211)	1,558,654
Municipal Communications Utility	5,976,879	891,731	6,868,610
Total Expenditures	<u>20,654,080</u>	<u>2,041,791</u>	<u>22,695,871</u>
Net Change in Net Assets	953,804	(3,569,920)	(2,616,116)
Net Assets at Beginning of Year	<u>17,684,388</u>	<u>45,995,135</u>	<u>63,679,523</u>
Net Assets at End of Year	<u>\$ 18,638,192</u>	<u>\$ 42,425,215</u>	<u>\$ 61,063,407</u>

**MUNICIPAL COMMUNICATIONS UTILITY
OF THE CITY OF SPENCER, IOWA
NOTES TO REQUIRED SUPPLEMENTARY INFORMATION –
BUDGETARY REPORTING
YEAR ENDED DECEMBER 31, 2010**

The budgetary comparison is presented as Required Supplementary Information in accordance with Government Accounting Standards Board Statement No. 41 for governments with significant budgetary perspective differences resulting from not being able to present budgetary comparisons for each individual utility.

In accordance with the Code of Iowa, Spencer Municipal Utilities annually adopts a combined budget on the cash basis for the Municipal Electric Utility, Municipal Water Utility, and Municipal Communications Utility of the City of Spencer, Iowa following required public notice and hearing. The annual budget may be amended during the year utilizing similar statutorily prescribed procedures. Encumbrances are not recognized and appropriations lapse at year-end.

**MUNICIPAL COMMUNICATIONS UTILITY
OF THE CITY OF SPENCER, IOWA
FUNDING PROGRESS FOR THE RETIREE HEALTH PLAN
FOR YEAR ENDED DECEMBER 31, 2010**

Year Ended December 31,	Actuarial Valuation Date	Actuarial Value of Assets (a)	Actuarial Accrued Liability (AAL) (b)	Unfunded AAL (UAAL) (b-a)	Funded Ratio (a/b)	Covered Payroll (c)	UAAL as a Percentage of Covered Payroll ((b-a)/c)
2008	12/31/2008	\$ -	\$ 22,881	\$ 22,881	0%	\$ 958,187	2.4%
2009	12/31/2009	\$ -	\$ 28,668	\$ 28,668	0%	\$ 986,933	2.9%
2010	12/31/2010	\$ -	\$ 36,624	\$ 36,624	0%	\$ 1,016,541	3.6%

See Note 9 to the accompanying Notes to Financial Statements for the plan description, funding policy, annual OPEB Cost and Net OPEB Obligation, and the funded status and funding progress.

**INDEPENDENT AUDITORS' REPORT ON INTERNAL CONTROL OVER
FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS
BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN
ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS**

To the Board of Trustees
Spencer Municipal Utilities – Municipal Water Utility
Spencer, Iowa 51301

We have audited the accompanying financial statements of Municipal Water Utility of the City of Spencer, Iowa (Spencer Municipal Utility) as of and for the year ended December 31, 2010, which collectively comprise the Utility's basic financial statements listed in the table of contents, and have issued our report thereon dated April 5, 2011. We conducted our audit in accordance with U.S. generally accepted auditing standards and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered Spencer Municipal Utility's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing our opinion on the effectiveness of Spencer Municipal Utility's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of Spencer Municipal Utility's internal control over financial reporting.

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and would not necessarily identify all deficiencies in internal control over financial reporting that might be significant deficiencies or material weaknesses. However, as discussed below, we identified a certain deficiency in internal control over financial reporting that we consider to be a material weakness.

A deficiency in internal control exists when the design or operation of the control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect and correct misstatements on a timely basis. A material weakness is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility a material misstatement of the Utility's financial statements will not be prevented or detected and corrected on a timely basis. We consider the deficiency in internal control described in Part II of the accompanying Schedule of Findings as item II-A-10 to be a material weakness in internal control over financial reporting.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether Spencer Municipal Utility's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grants, non-compliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of non-compliance or other matters that are required to be reported under *Government Auditing Standards*.

Spencer Municipal Utility's responses to findings identified in our audit are described in the accompanying Schedule of Findings and Questioned Costs. While we have expressed our conclusions on the Utility's responses, we did not audit Spencer Municipal Utility's responses, and accordingly, we express no opinion on them.

This report, a public record by law, is intended solely for the information and use of the officials, employees and citizens of Spencer Municipal Utility and other parties to whom Spencer Municipal Utility may report, including federal awarding agencies and pass-through entities. This report is not intended to be and should not be used by anyone other than these specified parties.

We would like to acknowledge the many courtesies and assistance extended to us by personnel of Spencer Municipal Utility during the course of our audit. Should you have any questions concerning any of the above matters, we shall be pleased to discuss them with you at your convenience.

Williams + Company, P.C.

Certified Public Accountants

Spencer, Iowa
April 5, 2011

**SPENCER MUNICIPAL UTILITIES
MUNICIPAL COMMUNICATIONS UTILITY
SCHEDULE OF FINDINGS
FOR THE YEAR ENDED DECEMBER 31, 2010**

Part I: Summary of the Independent Auditors' Results:

- (a) An unqualified opinion was issued on the financial statements.
- (b) A significant deficiency in internal control over financial reporting was disclosed by the audit of the financial statements and is considered to be a material weakness.
- (c) The audit did not disclose any noncompliance, which is material to the financial statements.

Part II: Findings Related to the General Purpose Financial Statements

SIGNIFICANT DEFICIENCY:

II-A-10 Financial Reporting – During the audit, we identified a immaterial cash deposit which could result in a material misstatement of cash and accounts receivable not initially identified by Spencer Municipal Utility's internal control. This amount was either not recorded or not properly recorded in Spencer Municipal Utility's financial statements. This adjustment was subsequently made by Spencer Municipal Utility to properly include or reclassify this amount in the financial statements.

Recommendation – Spencer Municipal Utility should implement procedures to ensure all accounts are properly identified, classified, and included in Spencer Municipal Utility's financial statements.

Response – We will revise our current procedures to ensure the proper amounts are recorded in the financial statements in the future.

Conclusion - Response accepted.

INSTANCES OF NONCOMPLIANCE:

No matters were reported.

**SPENCER MUNICIPAL UTILITIES
MUNICIPAL COMMUNICATIONS UTILITY
SCHEDULE OF FINDINGS
FOR THE YEAR ENDED DECEMBER 31, 2010**

Part III: Other Findings Related to Required Statutory Reporting

III-A-10 Certified Budget – Disbursements during the year ended December 31, 2010 did not exceed the amounts budgeted in the business type activities function.

III-B-10 Questionable Expenditures – We noted no expenditures that we believe may not meet the requirements of public purpose as defined in an Attorney General's opinion dated April 25, 1979.

III-C-10 Travel Expenses – No expenditures of Utility's money for travel expenses of spouses of Utility's officials or employees were noted.

III-D-10 Business Transactions – Business transactions between Utility and Utility officials and employees are detailed as follows:

<u>Name, Title and Business Connection</u>	<u>Transaction Description</u>	<u>Amount</u>
Tom Howe, Board Member Part owner of H & N Chevrolet	Maintenance & Repairs	945

In accordance with Chapter 362.5(10) of the Code of Iowa, the transactions with the Board Member do not appear to represent conflicts of interest since total transactions with each were less than \$1,500 during the year.

III-E-10 Bond Coverage – Surety bond coverage of Spencer Municipal Utilities' officials and employees is in accordance with statutory provisions. The amount of coverage should be reviewed annually to insure that the coverage is adequate for current operations.

III-F-10 Board Minutes – No transactions were found that we believe should have been approved in the Board minutes but were not.

III-G-10 Revenue Bonds – No revenue bonds/notes were issued to the Utility.

III-H-10 Deposits and Investments – No instances of non-compliance with the deposit and investment provisions of Chapter 12(B) and 12(c) of the Code of Iowa and the Utility's investment policy were noted.

III-I-10 Telecommunication Services – No instances of noncompliance with Chapter 388.10 of the Code of Iowa were noted.